

# AGENDA

## MILWAUKIE CITY COUNCIL WORK SESSION OCTOBER 5, 2004

### MILWAUKIE CITY HALL

Second Floor Conference Room  
10722 SE Main Street

### ***WORK SESSION – 5:30 p.m.***

A light dinner will be served.

### Discussion Items:

	<u>Time</u>	<u>Topic</u>	<u>Presenter</u>
1.	5:30 p.m.	Sanitary Sewer Utility Rate Analysis	Paul Shirey
2.	6:00 p.m.	Sewer Extension Strategy	Alice Rouyer
3.	6:15 p.m.	Ballot Measure 37 Discussion	Gary Firestone
4.	6:25 p.m.	Adjourn	

### Public Notice

- The Council may vote in work session on non-legislative issues.
- The time listed for each discussion item is approximate. The actual time at which each item is considered may change due to the length of time devoted to the preceding items.
- Executive Session: The Milwaukie City Council may go into Executive Session pursuant to ORS 192.660. All discussions are confidential and those present may disclose nothing from the Session. Representatives of the news media are allowed to attend Executive Sessions as provided by ORS 192.660(3) but must not disclose any information discussed. No Executive Session may be held for the purpose of taking any final action or making any final decision. Executive Sessions are closed to the public.
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- The Council requests that all pagers and cell phones be either set on silent mode or turned off during the meeting.

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**To:** Mayor and City Council

**Through:** Mike Swanson, City Manager  
Alice Rouyer, Community Development and Public Works Director

**From:** Paul Shirey, Engineering Director

**Subject:** Sanitary Sewer Utility Rate Analysis and  
Upcoming Sewer Master Planning Issues

**Date:** September 20, 2004, for October 5, 2004, City Council Work Session

### **Action Requested**

The following issues are being presented for Council review and direction to staff.

- Background on the volume-based sanitary sewer rates adopted in 2001.
- An assessment of the current fiscal health of the sanitary sewer utility.
- The impact on rates required to address sanitary sewer master planning issues:
  - Regional wastewater consolidation
  - Annexation and sewer service extensions into the Urban Growth Management Area

### **Background**

In September 2001, the Council adopted the consumption-based sewer rate. Previous to that change every user—regardless of their demand on the system—was assessed the same cost. The change resulted in bills that reflected different amounts depending on a customer's use of the system. In adopting this change in methodology, the Council directed that the revenue impact be neutral.

At the same time as it enacted the new consumption-based methodology, the Council also adopted a modest increase in the rate charged. Thus, even if the fixed rate had remained in effect, users would have seen an increase in their bill, and revenue would have increased.

The new consumption-based methodology and the rate increase were phased in over a 30-month period to reduce the rate spikes that can result when converting to a consumption-based

system. The final rate increase took effect in July 2003. From the beginning, customers have complained that sewer rates have gone up too much and have questioned whether the transition from fixed rates to variable rates has resulted in overcollection of sewer revenues.

The current financial health of the sewer utility is addressed based on an analysis completed in May 2004 by Financial Consulting Services Group (FCSG). In addition, the potential impact to sewer rates from two independent actions is also addressed. These are: a) regional wastewater consolidation planning and the cost impacts to the sewer utility from the potential decommissioning of the Kellogg treatment facility; and, b) the cost to extend sanitary sewer service to areas planned for annexation in Milwaukie's Urban Growth Management Area (UGMA).

## **SEWER RATE BACKGROUND**

### **1. Why was the basic sewer rate methodology changed from fixed to variable?**

Following adoption of a sewer rate increase in February 2000, Council directed staff to determine if a volume-based structure would be more equitable than the flat-rate method (see attached Council Minutes from September 4, 2001). Key issues identified at the time were:

- Conservation should be rewarded and encouraged;
- Billing based on residential customer winter usage is appropriate; and
- Transition to a new structure should be phased in over three years.

In addition to charging a more equitable fee for sewer services, the proposed rates were intended to maintain financial stability for the utility. Finally, the impact on City revenues was designed to be neutral. That is, the transition to a consumption-based system was not intended to generate additional revenue.

### **2. In addition to developing a more equitable rate structure that recognized differences in customer usage, was there a need for the utility to generate more revenue?**

Yes. As part of the rate design effort, a consultant was retained. The City's consultant, FCSG, completed an analysis and forecast of the financial performance of the sewer utility in June 2001 (attached). The study focused on ensuring that the redesigned sewer rate structure collected revenues sufficient to cover expenses and obligations. The analysis found that the City needed to moderately increase the amount of total revenue collected to sustain the fiscal health of the sewer utility. An increase in revenue beyond that collected under the fixed rate occurred for two reasons.

- a. An annual increase of about 3.9% for a period of three years was built into the volume-based rates. Even if the flat-rate structure had been maintained, a small increase in customers' bills would have been obvious.
- b. Beyond the 3.9% three-year annual increase for all customers, the average sewer customer would see a negligible change in their bill from the flat-rate to the volume-based structure. A below-average customer would see a decrease under the volume-based structure and an above-average customer would see an

increase in their bill. These “equity shifts” are the by-product and intent of a volume-based rate structure.

### 3. Why did Council adopt a three-step phase-in of the rates?

- a. The purpose of the three-year transition was to soften potentially extreme impacts on customers from the change to volume-based sewer rates. Under the flat-rate structure, all residences were paying \$36.25 bi-monthly for sewer service, regardless of the volume they discharged to the system.
- b. For example, a low-consumption household that discharged 6 CCF<sup>1</sup> (almost 4,500 gallons) to the sewer system paid the same amount as a house that discharged 20 CCF (almost 15,000 gallons) to the system. If the rate structure were changed to a volume basis in one step, the bill for a high-volume customer would go from \$36.25 to \$57.00, an increase of over \$20.
- c. Instead, the transition strategy manages that difference in three steps over three years to allow time for customers to either adjust their household budgets or respond by conserving indoor water usage to lower their bill. This three-year transition also meant that customers who had been subsidizing high consumption customers saw their bill decrease over the three-year time frame.
- d. The following tables illustrate the “equity shifts” by comparing three different customers, each with varying consumption patterns.

**Three-person household, two adults, one child**

	<b>FY 2001/02</b>	<b>FY2002/03</b>	<b>FY 2003/04</b>	<b>Pre-Volume- based</b>
Highest bill of the year	\$131.85	\$132.85	\$120.85	\$106.85
Sewer bill	\$40.90	\$52.80	\$57.00	\$36.25
Winter average <sup>2</sup>	17 CCF	22 CCF	20 CCF	21 CCF

**Two-person household, two adults, no children**

	<b>FY 2001/02</b>	<b>FY2002/03</b>	<b>FY 2003/04</b>	<b>Pre-Volume-based</b>
Highest bill of the year	\$74.35	\$81.10	\$100.60	\$75.80
Sewer bill	\$38.80	\$40.20	\$38.10	\$36.25
Winter average	14 CCF	13 CCF	11 CCF	14 CCF

**One-person household**

	<b>FY 2001/02</b>	<b>FY2002/03</b>	<b>FY 2003/04</b>	<b>Pre-Volume-based</b>
Highest bill of the year	\$66.05	\$71.45	\$61.30	\$63.65
Sewer bill	\$34.60	\$34.60	\$33.90	\$36.25
Winter average	8 CCF	9 CCF	9 CCF	10 CCF

<sup>1</sup> CCF = 100 cubic feet = 748 gallons.

<sup>2</sup> Winter average is the average amount of water usage during December-March, used to more accurately reflect discharge to the sewer system.

**4. Is the sewer utility collecting more revenue than it needs or than was originally intended?**

The sewer utility is collecting more rate revenue than it did in 2001 for two reasons.

- a. The sewer rates adopted as a part of the three-year transition included moderate annual increases (3.9% per year) needed in total sewer revenue in order for the utility to recover all of its annual operating costs and policy requirements (e.g., reserves).
- b. There has been a small amount of growth in both the number of customers (about 90 EDUs, or 1.5%) and the amount of volume they are discharging to the sewer system. The sewer rates, and hence total revenue, are now linked directly to both of these statistics. Volume-based billing will generate more revenue if water consumption exceeds use predictions.

May 2004 projections show that the sewer utility is not overcollecting revenue. On the contrary, the utility requires an immediate small increase (approximately 1.5%) to ensure that its annual revenues equal its annual operating costs and depreciation. More explanation is provided in question #7 below.

**5. Does the manner in which the City accounts for its sewer revenue affect the perception of overcollection?**

Probably. The City has three separate sewer-related funds: a) #540 Sewer Operation Fund, b) #550 Reserve for Future Capital, and c) #545 SDC Fund. These funds are intended to serve specific purposes. Due to the City's practice of keeping nearly all revenue in #540, the operating fund, it may appear to the public that the utility is flush with more cash than it needs. The consultant recommends that the City take advantage of the existing fund structure to better designate the purpose and intent of cash reserves. Staff will be implementing these budget recommendations in the FY 2005/06 budget.

- a. Fund #540 can be viewed as the utilities checking account. It is the fund that pays for the daily ongoing expenses of the utility: payroll, employee benefits, and supplies for the maintenance of the sewer utility. Normally this fund should not carry over a large balance, other than a 45-day operating reserve as a safety cushion for operations.
- b. Fund #550 can be viewed as both a savings account and checking account for current year capital projects. The savings account portion collects revenue needed for annual depreciation (a contribution toward replacing the system amortized annually). The checking account portion covers costs for annual capital projects and those planned for in the Capital Improvements Program (CIP) for the coming five-year period. FCSG recommends that much of the fund balance in fund #540 be transferred and reserved in fund #550. A minimum reserve in fund #550 is also recommended for capital cost contingency and/or emergency reserves.
- c. Fund #545 is the account used strictly for system development charge (SDC) revenue. Funds in this account may only be spent for SDC-eligible projects. Eligible projects are those that are the direct result of growth in the utility system and must enhance the capacity of the system. Given that Milwaukie is not

currently growing at a rapid pace, use of these funds will likely be limited to annexation or other growth-related projects.

**6. During the reexamination of the volume-based rate structure in 2003, why did staff recommend against adopting the third phase of the 2001 rate increase?**

In June 2003, even though rate revenue was sufficient to cover existing requirements for FY 2003/04, FCSG made it clear that, beginning in 2004/05, annual rate increases of 2-3% would be needed to meet rising operating costs and the capital funding policy.<sup>3</sup> Projected rate revenues exceeded budgeted operating costs at the time of the analysis. Given concerns about perceived “overcollection” of rate revenue since the switch to a volume-based system, staff and FCSG recommended that the utility forego the previously adopted 4.5% increase that was to become effective on July 1, 2003. Council did not concur with this recommendation and elected to implement the 4.5% rate increase to take effect on July 1, 2003, as scheduled.

**CURRENT FISCAL HEALTH OF THE SEWER UTILITY**

**7. What is the current fiscal health of the sewer utility, and are rates sufficient to meet required expenditures as budgeted for 2004/05?**

- a. FCSG has reviewed and modeled the revenue requirements for the next five years. The model incorporates operating revenues, operating and maintenance (O&M) expenses, capital funding needs, and any other expenditures and revenues associated with the sewer budget. An inflation rate of 4.5% (accounting for inflation in cost of materials and labor) and was determined by comparing past sewer budgets and considering recent higher-than-inflation-level price increases.
- b. Capital needs were estimated based on the current 2004-2009 CIP.<sup>4</sup>
- c. FCSG further recommended that the utility fully fund depreciation as a cash contribution to its capital reserves (fund #550). This has not been a regular or routine practice in Milwaukie; water rates were recently adjusted in order to address this issue.
- d. Results of the analysis include the following.
  - i. With mild rate increases to keep pace with inflation, sewer rates can generate sufficient revenue to fully fund operating expenses, capital needs, depreciation, and other expenditures associated with sewer operations without the issuance of debt.

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<sup>3</sup> At the time, the sewer fund was not funding depreciation; e.g., the estimated annual expense necessary to accrue a “savings account” that can be tapped to replace capital components (pipes and pumps) of the system as they wear out.

<sup>4</sup> An updated Sanitary Sewer Master Plan is scheduled for adoption in September 2004.

- ii. Beginning with the current FY 2004/05, small increases will be needed to cover inflation. The following table demonstrates the necessary rate increases to meet the needs of the utility.

**Table 1**  
**Projected Rate Increases to Remain Revenue-Neutral**

	2004/05	2005/06	2006/07	2007/08	2008/09
Annual rate increases	1.46%	4.31%	3.13%	3.11%	3.11%
Cumulative rate increases	1.46%	5.84%	9.15%	12.55%	16.05%

## **SEWER MASTER PLANNING ISSUES**

### **8. How will future annexation and sewer line extensions in our urban growth management area impact rates?**

The proposed Sanitary Sewer Master Plan identifies seven sanitary basins within Milwaukie's UGMA that are lacking sanitary sewer that are served by individual, private septic systems. These unsewered basins are located in the northeast corner of the UGMA and comprise about 10-15% of the total UGMA area. The balance of the UGMA is served with sewer by Clackamas Sanitary Service District #1 (CCSD#1). Upon annexation of those currently sewerred areas, cooperative agreements with CCSD#1 will need to be negotiated.

The utility has the option to use existing rate revenue to fund all, some, or none of the cost of extending service to new customers in newly annexed areas. Adding to the customer base of the utility will increase revenues and will spread the cost of capital and O&M across a larger base. This tends to lower unit costs and improves economies of scale, up to a point. These questions have yet to be fully analyzed; however, there are several ways to tackle the cost of service extensions.

- a. Local Improvement Districts (LIDs) may be formed for each of the seven subbasins lacking sewer in the UGMA area to the east of current city boundaries. This would place the cost burden entirely on those receiving new service and would not impact existing customers' rates.
- b. The utility could sell bonds and create separate customer classes whereby customers in newly annexed areas pay all or a portion of the cost of the new service. The utility could determine what portion, if any, of the cost would be borne by existing ratepayers. Providing a cost subsidy to the newly annexed customers has rate implications for the utility but not enough work has yet been done to quantify these. Subsidies can provide a positive incentive to lower-income households that require service. The City of Milwaukie will continue to seek Community Development Block Grant (CDBG) awards to fund sewer service extensions in areas that qualify.
- c. With direction from Council, staff will begin developing a financing plan and strategy for the unsewered areas in Milwaukie's UGMA.

**9. What action should the City take in anticipation of the potential consolidation of wastewater treatment services in Clackamas County and the potential decommissioning of the Kellogg treatment facility?**

- a. Clackamas County Sanitary District #1 and the Oak Lodge Sanitary District recently completed a study of the cost of providing wastewater treatment services to the urbanized county over the next 30 years. Five alternatives were explored, ranging from keeping each of the three north Clackamas treatment facilities operating to closing facilities in Milwaukie and Oak Lodge and consolidating wastewater treatment at the Tri-City plant in Oregon City. Elimination of the Kellogg plant has long been a desire of the City of Milwaukie.
- b. Council recently approved a resolution supporting option five, which consolidates all treatment at the Tri-City plant in Oregon City and closes Kellogg and Oak Lodge facilities. A decision by all the parties is anticipated by the end of the year. This will allow adequate time to design, finance, and construct the necessary treatment capacity within the next two to three years, in keeping pace with growth of urbanized northern Clackamas County.
- c. Closure (decommissioning) of the Kellogg plant has obvious near- and long-term advantages to the residents of Milwaukie, including redevelopment potential of the downtown riverfront. This has many benefits including an increase in Milwaukie's tax base. As "host" of the proposed consolidated treatment plant, Oregon City has already asked for a variety of inducements and incentives in exchange for the land needed to build the largest treatment plant in the region. These include reduced rates, an annual cash payment, and investments in creating quality park/recreation facilities adjacent to the new, expanded plant.
- d. A financial contribution from the City of Milwaukie to help defray a portion of the cost of consolidation and removal of the Kellogg facility from the riverfront will probably be necessary to achieve consensus among the participating jurisdictions. Assuming continuing capital investment, the Kellogg plant is deemed to have a useful life beyond the next few years. Because of this, there are users for whom the decommissioning of Kellogg imposes a cost, while at the same time decommissioning benefits Milwaukie. (The cost is the need to replace a plant that arguably has a remaining useful life.) By accepting some responsibility for bearing that cost, the City effectively meets one of the most potent arguments against elimination of the plant. For the purpose of analysis, staff selected a \$5 contribution as one possible option to consider.

**10. What is the impact on sewer utility rates of a contribution of \$5.0 million toward the closure of the Kellogg facility?**

FCSG conducted an analysis of the impact to Milwaukie sanitary sewer rates to raise five million dollars. Three probable scenarios were developed.

- a. **A \$1.0 million payment would be made in each of the next 5 years, beginning in FY 2004/2005, for a total of \$5.0 million.** This treats the annual payment as a capital project using the cash reserves from the Capital Construction Fund. The results indicate that a total of over \$3.42 million of revenue bonds would be needed to fund this scenario over a term of twenty

years. This figure includes the charges associated with issuing bonds. The following table demonstrates the necessary increases *over and above those needed to keep pace with the rising cost in operations and maintenance as detailed earlier in this memo.*

**Table 2**  
**Projected Rate Increases—Decommissioning the Kellogg Treatment Plant**

	2004/05	2005/06	2006/07	2007/08	2008/09
Annual rate increases	1.46%	4.31%	5.57%	7.08%	6.91%
Cumulative rate increases	1.46%	5.84%	11.74%	19.65%	27.92%

- b. **One lump sum payment of \$5.0 million would be made in FY 2008/2009 from the projected reserve balance and the issuance of \$3.3 million in revenue bonds.** The results indicate that the rate increases would be the same for all years as illustrated in Table 2, except in FY 2008/2009 where an increase of 11.3% would be necessary to cover debt service payments.
- c. **One lump sum payment of \$5.0 million would be made in FY 2008/2009 through the accumulation of reserves without incurring debt.** Under this scenario, the sewer rates would need to be increased by 12.5% per year for the next four years to accumulate this amount. This approach might be termed the “self-financing” method. Under this scenario, the rates would be temporarily increased to cover this one-time expense and would generate large amounts of revenue following this lump-sum payment.

## **Conclusions**

1. The shift from a fixed-rate billing structure to a volume-based structure has not generated excess revenue for the sewer utility. Customers who consume more water (discharging more to the wastewater system) have seen an increase in their sewer bills.
2. The utility should begin to “expense” depreciation and make deposits to its fund for future capital on an annual basis according to a depreciation schedule.
3. The current fiscal health of the sewer utility is good, but requires relatively small rate increases over the next five years to keep pace with inflation. The increases range from 1.46% to 4.31% and average just over 3% per year over the next five years.
4. Annexing new area to Milwaukie’s sewer service area will add customers and generate more revenue but will also increase operating and capital expenses for the utility. The dynamic between revenue and expenses has yet to be fully analyzed. There is some flexibility in funding options to extend sewer service to newly annexed areas.
5. In order to make a contribution toward the closure of the Kellogg plant and minimize impact on ratepayers, the utility would need to temporarily increase rates to fund a bond sale for this purpose. The bonds would be financed from the rates charged to users of the system. Rate increases range from 1.43% to almost 7% and average about 5% per year over the next five years.

### **Concurrence**

The Engineering Department has coordinated these issues with the City Manager, the Community Development and Public Works Director, the Finance Department, and Public Works Operations.

### **Fiscal Impact**

Impacts to the sewer utility will be in the form of rate increases needed to maintain revenue for approved operating and capital budgets and potentially to make payments toward decommissioning of the Kellogg treatment facility. The cost of extending service to newly annexed areas will need to be equitably managed for the benefit of all ratepayers.

### **Workload Impacts**

If rate increases are recommended, the Engineering and Finance Departments will manage the process. The billing department will continue to answer numerous customer inquiries about rates.

### **Alternatives**

1. Provide staff with direction on sewer utility rates.
2. Take no action.

### **Attachments**

- A. Sewer Rate Findings, May 27, 2004, FCSG
- B. Issue Paper on Appropriate Levels of Reserves, May 27, 2004, FCSG
- C. Council Minutes from July 1, 2003
- D. Sewer Rate Update Report for FY 2003/04, June 13, 2003, FCSG
- E. Sewer Rate/Billing Review Conclusions, December 18, 2002, FCSG
- F. Volume-based Sewer Rate Report to City Council, October 2, 2001
- G. Council Minutes from September 4, 2001
- H. Volume-based Sewer Rate Report to City Council, September 4, 2001
- I. Sewer Rate Study, FCSG, June 5, 2001



# Memorandum

**To:** Jay Ostlund, City of Milwaukie  
**From:** Jeanette Hahn, Nihat Dogan, and Ed Cebren, FCS Group  
**RE:** Sewer Rate Update for Fiscal Year 2004/2005

**Date:** May 18, 2004

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## Background and Scope of Work

In 2001, FCS Group performed a sewer rate study for the City of Milwaukie that included recommendations for changing to a volume-based billing structure. As a result of that study's recommendations, the City adopted a 3-year graduated implementation, during which the fixed charges decreased as greater reliance on volume-based rate revenue was phased in. During each of these annual rate structure changes, a small rate increase was also built into the structure to ensure that the utility continued to collect revenues sufficient to cover full operating, capital, and policy-related costs and obligations.

In June 2003, the City hired FCS Group to conduct an update to the sewer rate study, as a follow-up to the volume-based sewer rate implementation conducted for the City in 2001. Our scope of work for this update included reviewing and validating current and budgeted financial and customer data provided by the City, forecasting rate revenue requirements based on updated operating and capital needs, restructuring sewer rates as needed to continue policy goals developed in 2001 and recover sufficient revenues, and recommending an updated strategy for the utility as it enters the 2003/2004 fiscal year. For fiscal year 2003/2004, the City implemented its final rate step, in which the fixed portion of the rate dropped to \$15.00 per unit, and the volume charge increased to \$2.10 per hundred cubic feet (ccf) for residential and \$2.95 per ccf for commercial.

In April 2004, the City engaged FCS Group to evaluate its sewer rates and the financial condition of the utility as a follow-up to the forecast of rate needs completed in 2003 update and as an ongoing check-up stemming from the conversion to volume-based sewer rates initiated in 2001. Key questions to be answered in this review include:

- Why does the City collect more revenues although the volume based rates were intended to be revenue neutral?
- What is the appropriate amount of reserves the utility should maintain?
- What would be the effect of a \$5.0 million payment to help Kellogg go away in the next five years?
- The City is in the process of updating its sewer comprehensive plan. If the utility's capital needs go down, should the City change its sewer rates, and why?

- Comparison of sewer bills before and after the rate change for three different residential homes.

More specifically, FCS Group's scope of work included

- o Updating the existing revenue requirements model to assess the current financial condition of the utility and forecasted rate needs.
- o Developing alternative financial and rate forecasts under different assumptions, such as the level of capital spending, potential Kellogg decommissioning, the level of reserves targeted.
- o Describing appropriate reserve levels to target and effect of those policies on the City's sewer rates (provided as a separate issue paper)
- o Preparation of a comparison of sewer bills for selected customer accounts.

### **Data Sources and Key Assumptions**

The analysis used the following assumptions and data sources:

- o Beginning 2004/2005 Operating Fund balance is taken as \$2,975,000 per budget report dated April 30, 2004.
- o FY 2004-2005 beginning reserve for future capital (# 550) is based on year-to-date staff estimate (\$898,799) and projected transfers in the next two months (\$150,000). City staff also provided the beginning balance of the SDC Fund (# 545) (\$935,000).
- o 2005 capital improvement projects are taken from the Budget Proposal Report dated April 30, 2004. Capital improvement projects in 2006 and 2007 are kept as the same as 2003 rate study update. \$300,000 capital projects are assumed for 2008 and 2009. Project costs are inflated using 3% annual construction cost inflation.
- o Rather than using the budgeted rate revenues, the analysis used projected revenues. 2004 revenues are estimated based on 2003 actual revenues plus customer growth, plus 4.5% rate increase. Revenues in 2005 and thereafter are projected based on prior year revenues plus growth.
- o Expenditure projections are based on 2005 approved budget.
- o In order to avoid undue rate impacts while holding high levels of reserves, the analysis assumes that Kellogg loan would be paid from capital reserve. Hence it does not have a direct rate impact. Based on the utility budget, the City will pay \$350,000 in 2004/2005 as Kellogg Loan principal payments. Using the data from the prior update, it is assumed that the last principal payment for this loan will be \$150,000 in 2005/2006.
- o Depreciation expense in 2004 are assumed to be the same (\$134,000) as the prior rate study update.
- o Annual revenues from SDCs are assumed to be \$29,000.

- o Interest earnings rate was assumed to be 2%, reflective of current economic conditions.
- o Customer growth was kept at 0.05%.
- o Debt interest rates were assumed to be 4%, reflecting of the current market conditions.
- o Inflation was left at 3%. Given the interest earnings assumption of 2%, this is a conservative choice.
- o The expense budget is expected to grow with inflation.

The revenue requirements forecast projects utility needs through fiscal year 2008/2009, based on the City's fiscal year 2004/2005 budget, escalated by inflationary factors. (The detailed forecast is included as an attachment to this memorandum).

### **Results of Revenue Requirement Analysis**

The revenue requirement analysis forecasts the amount of annual revenue that needs to be generated by sewer rates. The analysis incorporates operating revenues, operating and maintenance (O&M) expenses, capital funding needs and any other identified revenues and expenditures related to utility operations, and it determines the sufficiency of the current level of rates.

The total CIP needs for the FY 2004/2005 - FY 2008/2009 period is over \$2.0 million. Our forecast indicates that all the capital needs can be met by existing and future cash reserves, with the utility still maintaining a healthy reserve at the end of the forecast period.

Based on the utility budget, the City anticipates total operating and maintenance expenditures to be \$2.91 million for FY 2004/2005 fiscal year. Inflationary increases in O&M expenses are projected for the rest of analysis period.

FCS Group projected 2004/2005 revenues to be \$2.96 million. The analysis used this amount as the basis for projections rather than budgeted \$2.84 million. FY 2002/2003 year-end actual revenues are escalated by assumed growth rate plus the adopted 2003/2004 rate increase of 4.5% to arrive at the FY 2003/2004 revenue projections. Revenue projections for the upcoming budget period (FY 2004/2005) and thereafter are derived simply by escalating this amount by assumed annual growth rates.

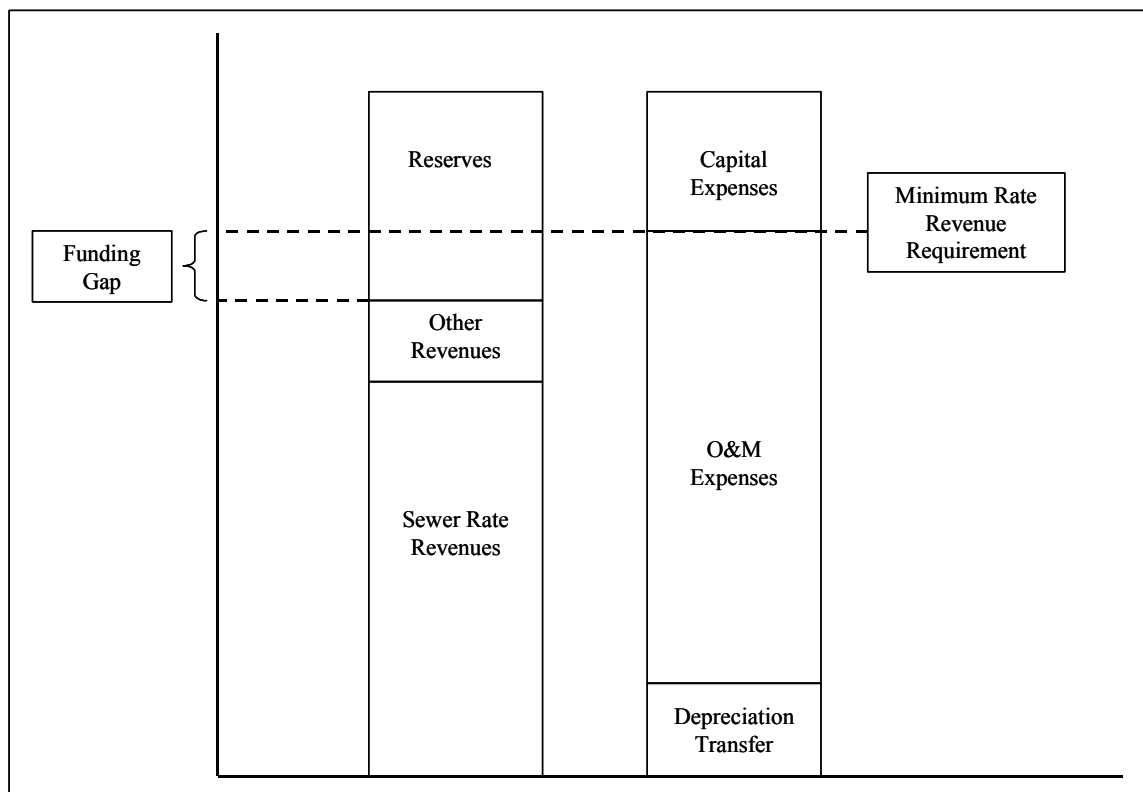
Our projections indicate that the City would need to make inflationary adjustments (increases) in its sewer service rates (see Exhibit 1 below). This finding is consistent with our prior rate study update. The detailed spreadsheet analysis is presented in the Attachment A.

#### **Exhibit 1 Projected Rate Increases**

	<b>2004/05</b>	<b>2005/06</b>	<b>2006/07</b>	<b>2007/08</b>	<b>2008/09</b>
Annual Rate Increases	1.46%	4.31%	3.13%	3.11%	3.11%
Cumulative Rate Increases	1.46%	5.84%	9.15%	12.55%	16.05%

These rate increases are driven by the assumed inflationary increases in the O&M expenditures and the City's policy of generating cash from rates on an annual basis to be used strictly for capital reinvestment in system infrastructure. That amount is linked to the utility's annual depreciation expense. This policy continues to be prudent fiscal management, giving the utility the capability to cash-fund capital improvements and demonstrate willingness and ability to repair, replace, and maintain capital facilities. As explained above, the utility has adequate reserves to finance its anticipated capital expenditures. The Exhibit 2 below demonstrates the utility's financial condition and our projections on a conceptual basis.

**Exhibit 2**  
**Projected Rate Increases**



### **Projections under Alternative Scenarios**

#### ***A. Lower Capital Improvement Program Costs than Anticipated***

The sewer utility is currently undertaking a master planning effort, which will likely modify capital improvement projects assumed in the Base Case analysis. As part of this study, the City asked FCS Group to assess the impact of a lower capital improvement need on rates. For this purpose, we assumed that the total CIP would be 20% lower than the base case in every year throughout the projection period.

As explained above, the utility has enough cash reserves to pay for its CIP. In other words, the projected capital-financing plan has no direct impact on the projected revenue requirements and

service rates. Therefore, lower capital expenditures will not have a major impact on the projection results, except the cash reserve for future capital construction would be higher compared to the base case projections.

***B. Payment of \$5.0 million over 5-years to help decommission the Kellogg Treatment Plant***

The second scenario analysis requested by the City was to assess the impact of paying \$5.0 million over the next 5 years to help the Kellogg Treatment Plant's move. We evaluated this scenario using three alternative payment plans. In the first alternative, we simply assumed that the City would pay \$1.0 million a year for the next 5 years, starting in 2004/2005 fiscal year. These payments are treated as if they were additional capital projects. In other words, it is assumed that the utility's available cash reserves in the Capital Construction Fund and SDC Fund would be used to make these payments and any deficiency would be funded by issuing revenue bond.

The results of this analysis indicate that the utility's available cash reserves would not be adequate to pay for anticipated capital projects and these payments. Therefore, we project that the utility would need to issue a total of over \$3.42 million in revenue bonds to make these payments and finance the anticipated capital projects. It should be noted that the amount of projected bond issues also includes issuance costs, funding a bond reserve, and meeting annual coverage covenants through rates.

As can be seen in Exhibit 3, servicing these bond issues would necessitate higher rate increases than the base case scenario. The results of this scenario are presented in the Attachment B.

**Exhibit 3**  
**Projected Rate Increases – Decommissioning the Kellogg Treatment Plant**

	<b>2004/05</b>	<b>2005/06</b>	<b>2006/07</b>	<b>2007/08</b>	<b>2008/09</b>
Annual Rate Increases	1.46%	4.31%	5.57%	7.08%	6.91%
Cumulative Rate Increases	1.46%	5.84%	11.74%	19.65%	27.92%

In the second payment alternative, we assumed that the City would make a \$5.0 million lump sum payment in FY 2008/2009. To make this payment, the City would have to issue a \$3.3 million revenue bond in FY 2008/2009. Under this alternative, projected annual rate increases are the same as the base case scenario with the exception of the last fiscal year. The City would need to increase rates by 11.3% in FY 2008/2009 to service debt payments. This large increase results in a 25.3% cumulative rate increase in the analysis period.

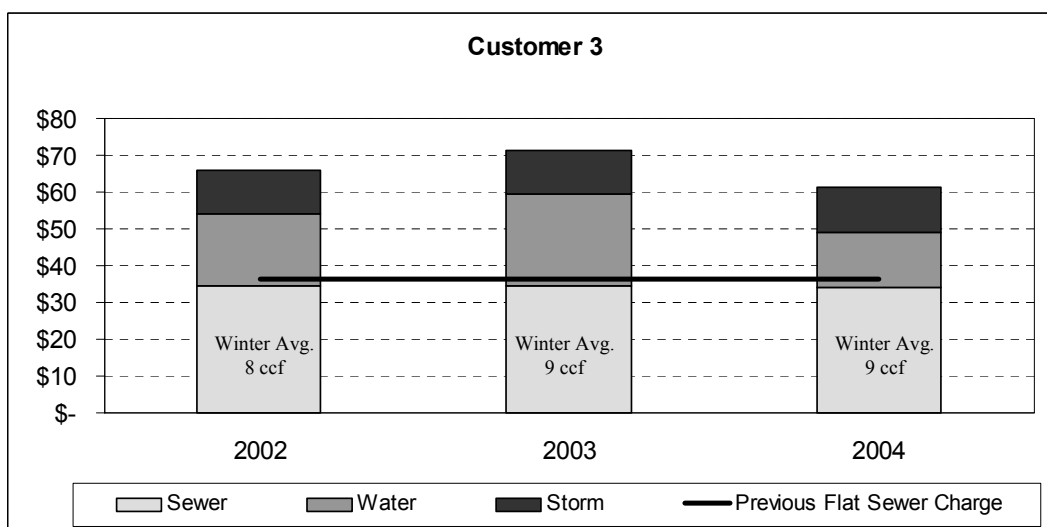
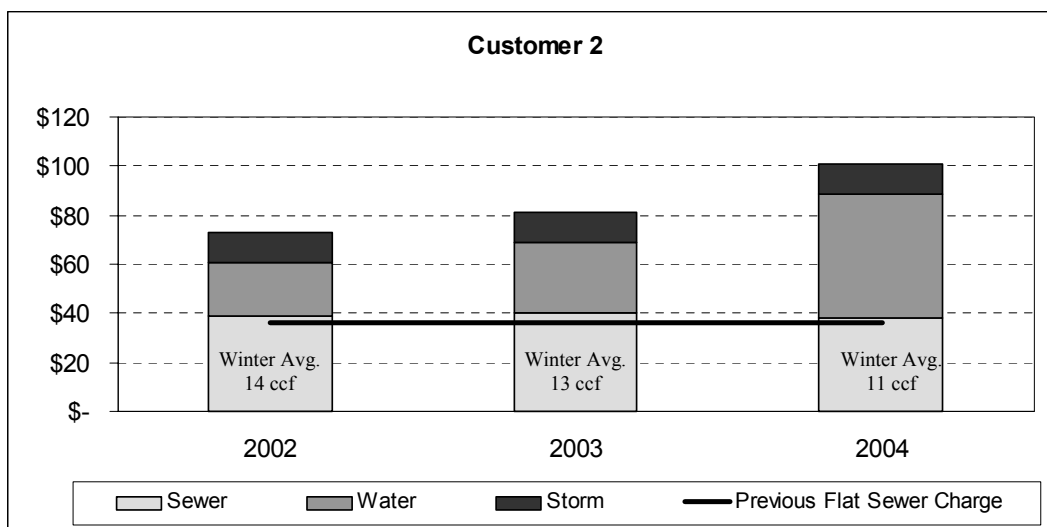
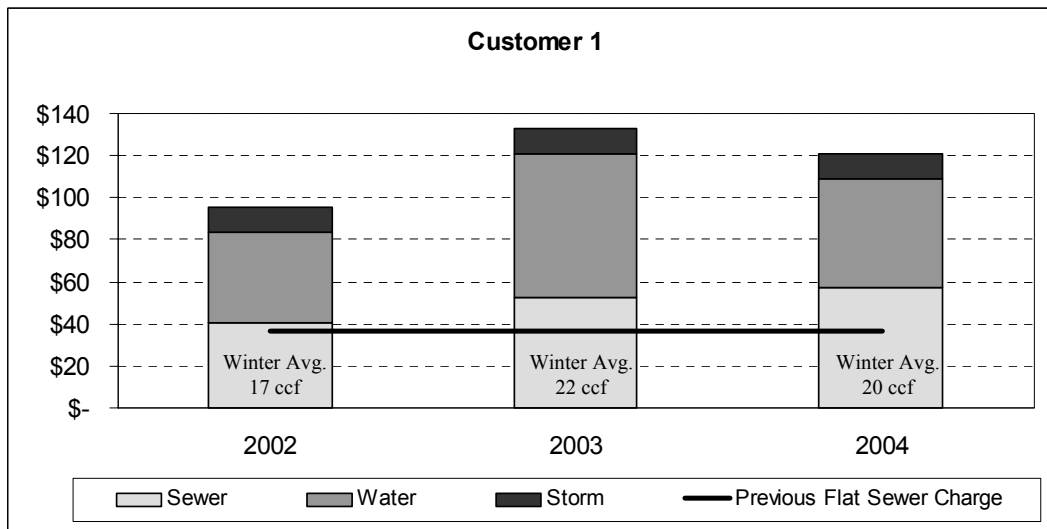
The last alternative we evaluated is a derivative of the above scenario. We assumed that the utility would try to accumulate reserves by larger rate increases than needed and use its accumulated reserves to make the \$5 million payment in 2008/09, rather than issuing debt. The City would need to increase its sewer rates by 12.5% per year over the next four fiscal years to accumulate adequate reserves. It should be noted that under this scenario the rates would need to be artificially increased and the City would be generating large amount of cash following the payment for decommissioning Kellogg, unless rates were recalibrated thereafter.

### **Customer Bill Impacts of the Volume Based Sewer Rates**

The City also asked FCS Group to evaluate customer bill impacts of the volume based sewer rates using three sets of specific customer account information provided by the City. A comparison of sewer bills under the volume based rates and previous flat sewer charge for each customer account is provided in Exhibit 4 below.

As can be seen from the Exhibit, high water users pay a higher sewer bill under the volume based sewer rate structure. On the contrary, under the flat rate structure, everybody paid the same price regardless of water consumption. In other words, low water users subsidized high water users, although they placed a lower demand to the system. The volume based rate structure eliminates (or at least reduces) these subsidies and recovers cost of sewer service from customers more equitably.

### Exhibit 4 Customer Bill Impacts of Volume Based Sewer Rates



## Findings & Conclusions

The study's findings can be summarized as follows:

- Following the City's transition to the volume based rate structure, the City had concerns that the volume based rate structure generated more revenues than the rate study's original projections. In 2002, FCS Group audited the utility billing system to ensure that bills were accurately calculated by the system to address these concerns. The findings of this review process had been provided to the City as a memorandum. As part of this rate update exercise, City staff and FCS Group revisited this issue. It should be noted that a better assessment of the level of revenues is to compare revenues generated against utility's needs to operate as a financially viable entity. The key point is that level of revenues is necessary and appropriate to pay for the utility's operating and maintenance cost and to fund the depreciation expense for capital reinvestment in system infrastructure. Based on the 2003/2004 and 2004/2005 budgets and this study's forecasts, it can be concluded that the utility is in fact not over-collecting through rates.
- Appropriate reserve levels for the sewer utility vary based on specific circumstances under which the utility operates. A brief, conceptual discussion of potential factors that might affect appropriate reserve levels the utility should maintain is provided in a separate issue paper. However, experiences from similar utilities and industry standard provide a rule of thumb in determining the appropriate reserve levels. Usually operating reserves for wastewater utilities are set at 30-60 days of cash operating expenditures. In our rate analysis, we assumed a 45 days of cash operating expenditures as the minimum operating reserve target. We believe that, based on our experience, this is a reasonable assumption.
- Based on the available information and study assumptions documented above, the City would need to make inflationary-level increases to its sewer rates to cover its operating and maintenance costs and to satisfy its policy decision of generating cash from rates (equal to annual depreciation expense) to be used strictly for capital reinvestment in system infrastructure. This finding is consistent with FCS Group's prior rate study update conducted last year.
- The results of our analysis indicate that the projected rate increases under the Base Case scenario would not be affected, should the City's updated sewer comprehensive plan determines that its capital improvement needs are less than anticipated in the Base Case. Lower capital needs would only affect the amount of utility reserves used, and hence result in higher available reserves for future years.
- A \$5.0 million payment to help decommission the Kellogg Treatment Plant would result in higher annual rate increases. The timing and source of this payment will determine the required rate increases. Based on the three alternatives evaluated, we show that cumulative rate increases needed by 2008/09 range from 25.3% to 60.2%.
- The comparison of customer bills shows that the volume-based sewer rate structure improved the equity achieved among customers. High water users pay higher bills, and

low water users pay lower sewer bills as opposed to flat sewer rates. The current sewer rates are operating as intended.

# **City of Milwaukie**

## **Wastewater Utility**

### **Issue Paper on Appropriate Levels of Reserves**

**Issue:** As part of the rate study conducted by the Financial Consulting Solutions Group, Inc. (FCS Group) for the City of Milwaukie's (City) Wastewater Utility (Utility), the City requested an evaluation of the appropriate levels of reserves the Wastewater Utility should maintain. This issue paper provides a general discussion of purposes and use of reserves and issues to be considered while determining the appropriate levels of reserves.

#### **Background and Analysis:**

Prudent financial management of a utility involves an effective management of utility reserves and establishment of reserve policies. Key objectives of reserve policies can be summarized as follows;

- Minimization of reserve levels while limiting concurrent risk
- Managing reserves to mitigate adverse impacts on rates due to increasing or decreasing reserve levels, and
- Maintaining creditworthiness of the utility by avoiding any indication of weakening financial controls.

Utility reserves have two major components; operating reserves and reserves related to the management and construction of utility fixed assets (capital). Other types of reserves can also be appropriate, depending on specific legal requirements and policy objectives. These can include bond reserves as defined by bond ordinance, or capital replacement reserves as dictated by policy. This issue paper focuses on operating reserve and plant emergency reserves.

#### *Operating Reserves*

The purpose of operating reserve is to satisfy the utility's working capital needs and to provide a cushion for operating contingencies.

The working capital reserve provides for fluctuations in revenues and expenses, both in terms of short-term fluctuations and in terms of annual revenue cycles. The utility's revenue stream follows billing cycles and seasonal usage patterns, while expenditures are incurred on various bases; biweekly, monthly, and random. The variations in revenue (cash receipts) stream and payment streams each create a need for working capital

reserve, since they do not necessarily coincide. Major drivers of working capital need are as follows:

- **Revenue Cycle:** Variations in revenue due to billing periods and/or seasonal usage patterns. The City of Milwaukie's residential sewer customers are billed based on the winter average usage, whereas commercial accounts are billed based on actual usage. Therefore, seasonal variations in revenues should be limited, since residential accounts constitute a larger portion of the customer base.. Besides, the City's fiscal year starts in July. Revenues generated from commercial accounts should be higher in summer months. Hence the utility should normally start the fiscal year with higher revenues. This should provide a working capital cushion in the remainder of fiscal year, when monthly revenues are lower. Therefore, this component should not necessitate large working capital reserves.
- **Payroll Cycle:** Timing of fixed cash requirement for payroll as related to revenue cycle. Payroll cycle creates discrete cash requirements in semi-month intervals. To reflect this, cash reserves should be sufficient to accommodate the payroll pattern.
- **Wholesale Expense / Revenue Lag:** Delay between wholesale costs and corresponding sewer revenues.
- **Wholesale Cost Variability:** Variability of wholesale costs due to rate/payment structure and/or usage patterns. If payments to Kellogg for treatment services are tied to winter average usage, then revenues and wholesale expenses will follow a similar pattern. If this is the case, then a potential revenue decline will be offset by decline in expenditures. On the contrary, if the payments to wholesale purveyor are tied to actual flow or if they are fixed installment payments, then the utility's risk would be higher. Then higher reserves would be warranted for this component.
- **Debt Service Accrual:** Allowance towards next transfer into restricted bond repayment accounts
- **Miscellaneous Reserve Components:** Additional reserve levels appropriate for cash flow management

The operating contingency reserve is intended to provide a cushion against a poor performance against budget, either due to reduced revenues or increased expenditures. The availability of operating contingency reserve allows for more realistic financial planning, without undue conservatism in estimating revenues.

#### *Plant Emergency Reserves*

The plant emergency provides a hedge against a system failure at some anticipated level. A system failure could be failure of a major facility or a piece of equipment. It is not practical to reserve against major catastrophic events, such as earthquakes or structural failures, but more moderate (and potentially more frequent) events such as a pump station failure. The intent would be providing the funds needed on a short-term basis to respond to such extraordinary events. Some, but not all, plant failures are also protected by insurance. Therefore, the plant emergency reserve should focus on uninsured assets.

A reasonable plant emergency reserve level could be based on the cost of a major repair or replacement, or alternatively based on a percentage of fixed assets. The level of plant emergency to be protected against through reserves is ultimately a matter of judgment and policy. It will depend on the amount, age and conditions of system assets as well as other factors. For example, replacement of a pipe underneath a major highway would be a lot costlier than replacing a pump.

### **Other Considerations**

Determination of appropriate level of reserves would also be dependent on other factors, such as availability of other funds that could be tapped for this purpose. These funds could be a citywide contingency fund or reserves maintained for other utilities. Maintaining separate reserves for each utility protects against cross-subsidy, thereby retaining rate equity for each utility. However, it also results in higher reserve targets, with more funds retained than are otherwise needed.

Reserves can be reduced by sharing risks among utilities. This does not require that reserves actually be consolidated into a single fund, but simply that individual reserve targets reflect the strength provided by the availability of cross-utility support. Under this scenario, cash shortfalls in one reserve could be funded through inter-utility loans, to be repaid from future rates.

### **Recommendation**

The appropriate reserve levels can be determined by a detailed assessment of each reserve components explained above. This assessment would also consider overlaps between the components, potential counter-balancing impacts, and other sources that could be used if necessary. It would heavily rely on data availability and require a lot more detailed analysis than undertaken at this time.

However, experiences from similar utilities and industry standard provide a rule of thumb in determining the appropriate reserve levels. Usually operating reserves for wastewater utilities are set at 30-60 days of cash operating expenditures. In our rate analysis, we assumed a 45 days of cash operating expenditures as the minimum operating reserve target. We believe that, based on our experience, this is a reasonable assumption.

We did not assume a plant emergency and/or capital construction reserve.

## **MINUTES**

### **MILWAUKIE CITY COUNCIL JULY 1, 2003**

#### **CALL TO ORDER**

The 1913<sup>th</sup> meeting of the Milwaukie City Council was called to order by Mayor Bernard at 6:00 p.m. in the City Hall Council Chambers. The following Councilors were present:

Councilor Lancaster

Councilor Loomis  
Councilor Stone

Staff present:

Mike Swanson,  
City Manager  
Gary Firestone,  
City Attorney  
Alice Rouyer,  
Community Development/  
Public Works Director  
Mary Rowe,  
Human Resources Director

Paul Shirey,  
Engineering Director  
Jay Ostlund,  
Associate Engineer  
Jeff King,  
Project Manager

#### **PLEDGE OF ALLEGIANCE**

#### **PROCLAMATIONS, COMMENDATIONS, SPECIAL REPORTS, AND AWARDS**

**Mayor Bernard** read a list of people involved with making the Centennial Festival success. Ed Zumwalt expressed his appreciation to Mayor Bernard and all those who helped put on a very organized event. He briefly discussed the riverfront event being planned for July 26 that will include music, dragon boat exhibition, and fireworks.

#### **CONSENT AGENDA**

**It was moved by Mayor Bernard to move item VI.C – Cost of Living Adjustment for Non-represented Employees to the consent agenda. The motion died for lack of a second.**

**Councilor Stone** had questions on consent item D – A Resolution Authorizing the City Manager to Sign Annual Purchase Orders Exceeding \$25,000.

**It was moved by Councilor Lancaster and seconded by Councilor Stone to adopt the consent agenda, which consisted of:**

- A. City Council Minutes of June 10 & 16, 2003;

- B. Bid Award for 2003 – 2004 Waterline Improvements, Phase 1; and
- C. Resolution No. 29-2003: A Resolution of the City Council of the City of Milwaukie, Oregon, Amending Resolution No. 29-2001 and Amending Sewer Service Charges for Properties Receiving Service from the City of Portland; Classifying the Fees Imposed by this Resolution as Not Subject to Article XI, Section 11B of the Oregon Constitution.

**The motion to adopt the consent agenda passed unanimously among the members present.**

## **AUDIENCE PARTICIPATION**

There were no participants.

## **PUBLIC HEARING**

None scheduled.

## **OTHER BUSINESS**

### **Sanitary Sewer Volume Based Billing -- Resolution**

**Ostlund** presented the staff report. In September 2001 Council adopted the sanitary sewer volume based rate structure. On January 21 of this year, staff provided an update on the rate structure. At that time, the City was seeing revenues in excess of what had been projected in 2001. Jeannette Hahn, Financial Consulting Solutions Group (FCSG), provided the consultant's report. He pointed out an additional resolution that would increase the minimum lifeline use.

**Hahn** provided an overview of the study and the 3-year transition to volume based sewer rates. The City started at a rate of \$29 per unit and is now currently at \$22 per unit. The final transition would drop the rate to \$15 per unit, complete the transitions, and have an appropriate proportionality in a volume-based rate structure. In that 3-year transition, there were revenue increases built into the rate changes. Not only did the fixed rate drop and the volume rate increase, but incremental, additional revenues are generated to stay on track with inflation. Residential living units are charged \$22 and \$1.40 per ccf of metered water volume. The earlier adopted rate of \$15 would go into effect on July 1, 2003 with a variable charge of \$2.10. Reliance is shifting to volume revenues. Implicit in that change is a 4.5% increase in revenues, so rates would generate more revenue than currently being collected.

FCSG conducted an analysis that looked at preliminary budgeted operating expenditures for the utility, ongoing capital expenditures through 2008, fiscal policy requirements, and any projected debt requirements to complete the capital program. FCSG recommends the Council not adopt the 4.5% rate increase. The sewer fund has a healthy balance with about \$2 million cash on hand. The user charges are consistent

with the ongoing operating costs, labor, treatment, and maintenance. In the future, the City should assess how that fund balance is being used and how added levels of service and inflation are impacting operating costs. As costs increase, the City may see the need for annual inflationary increases which may in the future be 2% - 4%.

In terms of rate structure, Milwaukie already has the mechanism in place, and Hahn recommended the City complete its transition to a volume-based structure by assuming the \$15 fixed charge and calibrating the volume charge. She recommended after that to continue monitoring customer volumes. The 2001 projections were under what the City is actually collecting at this time. The billing system was audited and there did not seem to be any problem in the software. It turns out the customer volumes are actually higher, so the City is collecting more revenue. Currently, the City collects about 41% of its revenues from the residential class volume charges, and when the final step is taken, the number will increase to 59%. There will be a similar increase in the commercial sector. Monitoring customer patterns will continue to be important in this utility.

FSCG recommends a \$15 bi-monthly charge for a single-family house with \$1.96 per ccf. Low income residential would continue to see that discounted by half. The commercial rates would also be recalibrated slightly to make sure revenues would not increase. She provided a table showing how residents would be impacted. The average customer uses about 12 ccf, so under the current rate the bill would be about \$38.80. Under the recommended rates she just discussed, the bill would be about \$38.52. The average customer will not see a substantial change in his/her bill because the change is supposed to be revenue neutral. Completing the transition continues to have a positive impact on low volume users, and high volume users will see an increase in their bills. This will put the rates in the right proportions with a lower fixed rate and complete what was begun in 2001.

In summary, the recommended action is to forego the previously adopted 4.5% increase and amend the adopted rate structure; complete the rate restructuring; and continue to monitor the cash reserves. The upcoming master plan will identify capital improvements and replacements to be made to the system. The fund balance is a benefit to the customers as long as the City uses it to reinvest in and proactively maintain the infrastructure. Over time those cash reserves will fall as needs are identified. In summary the proposed rate structure is to drop the fixed rate to \$15 and to amend the previously adopted volume rate.

**Councilor Lancaster** said Hahn characterized the sewer fund as being healthy with a \$2 million balance for capital projects. He asked what projects are planned and what can be reasonably anticipated for future projects. These would be in respect to the decommissioning costs for the Kellogg Treatment Plant. There may be some accelerated costs, and Lancaster wanted to know if those were incorporated in future planning.

**Ostlund** said the capital projects were adopted in the capital improvement plan. The master plan will address those needs mentioned by Councilor Lancaster.

**Swanson** said the City is at the front end of a process that will take about eight months to determine wastewater treatment options in the entire north area. One of the three options being considered is the decommissioning of Kellogg. The problem is an entire process must be gone through to decommission a plant. The honest answer to Councilor Lancaster's question is probably "no", but those costs will be developed over the next year.

**Councilor Lancaster** raised the issue because there will be some significant costs related to decommissioning Kellogg. He recalled a healthy, unexpected treatment bill in excess of \$1 million. In terms of what is being considered additional revenue, perhaps the City should pay itself back for that unexpected bill before considering a rate cut. If he understands, the increase is not a function of the rate structure itself but a function of an unexpected increase in consumption. It still seems revenue neutral to him since usage is higher than expected. This is what generated the additional revenue. He sees no fault in the structure itself. Hahn said the average for the average for all users is 12 ccf, and Councilor Lancaster asked if there was any data that speaks to what the average is for customers with no history.

**Hahn** replied customers are charged a minimum of 4 ccf until history is established.

**Councilor Lancaster** understands the recommendation is to change the minimum to 12 ccf for all users.

**Ostlund** said the average for all users is approximately 14 ccf. The Citizens Utility Advisory Board (CUAB) recommended adopting 12 ccf as the rate people would pay under the old system with the flat rate. The City initially established the 4 ccf because it did not want to overcharge those residents. Staff is now finding actual consumption is higher. The 12 ccf is a compromise.

**Hahn** said it is common to set the minimum consumption at the average. The 4 ccf was done at the time in lieu of having better data. The 12 ccf is closer to typical usage.

**Mayor Bernard** said Councilor Lancaster brought up a good question about the surprise bill from the Service District for the update of the Kellogg Treatment Plant. He asked Rouyer how that was funded.

**Rouyer** said the City has an intergovernmental agreement (IGA) with Clackamas County that allows up to a 10-year repayment. The schedule is about \$135,000 annually. This year, since there was a little extra revenue, staff accelerated the payment up to \$400,000 while making a healthy transfer into the reserve account. As Councilor Lancaster indicated, Milwaukie needs to think about the future and what might happen to Kellogg. There are between 2 and 5 years left to pay on that extra capital payment.

**Mayor Bernard** understands this rate anticipates paying that bill off in 2 – 5 years at a lower rate. He asked the interest.

**Rouyer** said it is very low. This is an important question to ask each year -- should the money be put in the reserve and continue paying the low interest? This year, staff decided to accelerate the payment and put some in reserve.

**Councilor Lancaster** said it seems to him the rate structure is good and going in appropriate direction. The only differential is that people's utilization increased, and they are being charged for that additional volume. He thinks it is appropriate to keep the structure and use the additional revenue to accelerate the payoff of the unexpected bill, and anything beyond that is put in reserve for anticipated use. Milwaukie's economic future literally depends on moving that treatment plant, and the City needs to have funds to make sure that happens.

**Mayor Bernard** tended to agree with Councilor Lancaster. He has heard concerns from people that their bills are so much higher while the fact is they are actually being billed for what they use. Milwaukie's water rates are substantially lower than Portland. He suggested not changing the rates and putting money aside in the reserve fund to help aid in decommissioning the sewage treatment plant.

**Councilor Loomis** said during the Centennial Festival he heard complaints about the sewer charge and how it had increased. The whole idea was revenue neutrality. If more is coming in, and the City is trying to save money to get rid of a plant that is working, he does not think the citizens should have to pay extra without being asked. He would like to see Kellogg gone too. That money should be used to maintain the system, and citizens should not have to pay extra.

**Councilor Lancaster** said customers are not paying extra. They are paying for what they use. Based on the data he has seen, high users have been subsidized by everyone else. All that has been done is to restructure the billing process. The minimum charge covers those who use little water, and those who do not conserve and use high volumes indiscriminately are now going to pay for their share of this very precious commodity. Customers are not being charged more; they are being charged for what they use. If usage had been the same as tracked in the past, there would have been no additional revenue. It is strictly a result of increased utilization. That is appropriate revenue generation in his opinion.

**Councilor Stone** said they are indeed paying more; their bills are higher. She totally agrees that they are paying for what they use. They have a certain amount of control over that to offset their bills if they chose to be conservation minded. She actually likes the idea of volume-based rates. It is more fair, and she supports it.

**Mayor Bernard** called for a motion, and none was made. The sanitary sewer rate schedule will not be revised.

It was moved by Councilor Lancaster and seconded by Councilor Stone to adopt the resolution altering the ccf rate for customers with no history based on the Citizens Utility Advisory Board recommendation to a rate of 12 ccf. Motion passed unanimously among the members present.

**RESOLUTION NO. 31-2003:**

**A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF MILWAUKIE, OREGON, AMENDING RESOLUTION 29-2001 AND 37-2001 RELATING TO SEWER RATES AND MINIMUM LIFELINE USAGE.**

**Mayor Bernard** suggested applying the additional cash flow to the debt with funds reserved for future efforts to decommission the Kellogg Treatment Plant.

**Councilor Lancaster** suggested an article in *The Pilot* reminding people their rates are based on water use and encouraging them to conserve.

**Firestone** asked for a matter of clarification that Councilor Lancaster's motion was to adopt the resolution included in the packet relating to customers with no water data.

**Councilor Lancaster** said that was correct.

**North Main Mixed Use Redevelopment Project Update**

**King** provided the staff report updating the City Council on the status of the North Main Street Redevelopment Project. In April, the citizen selection committee recommended Peak Development for the project. Council accepted that recommendation and directed staff to proceed with negotiations. There are several components to the process: design, financing, and the memorandum of understanding that gives exclusive negotiating rights and outlines the duties and responsibilities of both parties.

At this point, staff has been meeting with Peak Development twice a month, and progress is being made on the design aspects. Several sessions are scheduled for July during which three or four design options will be considered. Staff is proposing to reconvene the North Main Developer Selection Committee in early August to provide input.

The City Council concurred with that proposal.

**King** said staff further proposes a community outreach program, including an open house, in September and October. The timetable is to carry out the legislative process from October through March with the Planning Commission, Design and Landmarks Commission, and City Council with construction starting about May 2004. Construction is anticipated to take about one year. King briefly discussed the retail elements of the project and potential for Metro grants.

**Councilor Stone** asked in terms of a marketing strategy if Peak development is going to be doing the marketing for the retail space or will the City invest time and money to seek appropriate retail?

**Mayor Bernard** spoke with Peak Development about this issue because the community is clear in its desire to have the development include a specialty grocery store. There is no agreement with Peak yet. Peak indicated in all of its developments, retailers come in at the beginning, but few of the original people stay with the project. Usually the retail transitions to higher quality. It is a fluid process. Mayor Bernard offered City help by putting up a sign. He has heard a lot of interest at the Sunday Market from people interested in the residential portion of the development. While the market study shows a specialty grocery would work, it is rather early to get involved.

**Councilor Stone** understands the answer to her question is Peak is more responsible for marketing strategy than the City.

**King** said the City did provide Peak with a market study done last year, so that offers some value. The City is also offering signage. Most of the cost in the specific recruiting will be borne by Peak who will be the long-term owner. Peak is here to stay and is putting in some of its own equity and reinvesting its development fee. Peak reiterated at this very early stage a retailer may provide a letter of intent, but this is a very lengthy process in which things can change. There is always the concern that a single user taking up most or all of the retail space will drive the project. Peak will keep the City apprised every step of the way. One possibility that has been discussed is a very nice restaurant and microbrewery that could be a nice fit. The City may tour a similar business in Gresham.

### **Consider Cost of Living Adjustment for Non-Represented Employees**

**Swanson** said the proposed action is to adopt that portion of the pay table that applies to non-represented employees which includes management, confidential, and seasonal employees, with 3% cost of living increase. He discussed the negotiations with MPEA and AFSCME that resulted in contracts that reflect a 3% increase in these bargaining units effective July 1. That means represented employees receive a 3% salary increase effective today. The non-represented employees are essentially management or confidential employees or employees who are not full time to the extent that they are represented by one of the bargaining units. None of these employees are eligible for the cost of living adjustment negotiated on behalf of the two bargaining units. He recommends the non-represented employees be granted the same 3% cost of living effective July 1.

**Swanson** discussed the reasons for his recommendation. To be competitive, the City tries to maintain a pay system that maintains some equity with other local governments of similar size and similarly situated. Additionally, the City tries to maintain an internal equity between positions. For example, one would not want the police captain's salary to be static when officers consistently receive a 3% increase through the MPEA

contract. This tends to reduce incentive for someone to be in management. The second reason is over the last few years members of the management group have been asked to assume different roles. At the same time, positions are being reduced. For example, this year a management position was lost at the library. The job duties did disappear; others had to pick them up to provide service. The library lost a \$90,000 employee, and he is looking at increasing the two remaining senior librarians by 3%. The community development director, for example, has been asked to assume a significant role in the North Main Redevelopment Project. Everybody has responded.

**Swanson** asked in order to maintain internal equity and to recognize that additional effort is being asked as the organization downsizes that the non-represented employees be grant this 3% cost of living adjustment similar to that granted to the represented employees. The money has been budgeted but will not be released until the Council approves the pay table. If not spent, it would go into the balance of the various funds. He estimated this would cost about \$40,000 which includes salaries, FICA, etc. The expense is not just out of the general fund.

**Councilor Loomis** asked if this cost of living is standard? Does it happen every year, or has it been a while since these people got a raise?

**Swanson** said Council approved the recommendation last year. For some reason in the past the police chief and community development director were not included, but his recommendation includes those positions.

**Councilor Loomis** does not disagree these people are doing more, and it sounds like they are deserving. We are going through budget cuts. Just being on Council a short time and being involved in School District budget, there seems to be a real trust issue between the public on both counts. Citizens do not trust us; and we do not trust them to do the right thing. He hears they will never vote for the tax increment, road maintenance, and things like that. It is not a whole lot of money, but Councilor Loomis believes it chips away at that trust. How can you give a raise when you say you don't have any money? That is the thing he hears a lot, "I'm going to vote no because they have the money." It is a little thing, but he knows from the time he has spent on Council a time will come when the City has to ask for money. The citizens are in charge and then the people. He has heard Councilors talk about representing the people who voted for them. He thinks Council needs to look at representing everyone, not just the people who voted for them. He thinks long and hard about this all the time. He wants to vote yes, but it is really hard for him to believe the people want him to do that.

**Councilor Lancaster** appreciated Councilor Loomis's comments. The reason he asked to pull this item from the consent agenda was to ensure key directors were included. From his perspective, which is typically both a business and citizen point of view, there are two issues. There is merit pay, and there is cost of living. The whole intent of cost of living is to create some sort of compensatory index that does not cause buying power to erode. The merit pay speaks more to Councilor Loomis's comments about saying on one hand there is no money while giving employees big raises. That is

not what we are doing here. We are keeping the current employees somewhat level with today's economy. They are being asked to do more and are doing so with fewer resources. To him it becomes a critical issue of retaining quality employees. Milwaukie does not pay the highest salaries in the region already. The City tends to be a training ground for people to get experience and then move on to a better paying job doing the same thing. For him, adequate cost of living and addressing the compression issue is critical to retaining quality employees. In his mind, it is essential it is done and make sure the management team is part of that. The city manager chose not to take a pay increase last year, and Councilor Lancaster will not accept his not taking a cost of living increase. From his perspective it is critical to the City's staying sound as a business entity.

**Swanson** understands what Councilor Loomis is saying. Trust was the thing he saw as most in the need of repair when he took this position. When he comes before the City Council and recommends an increase, he also realizes this is not a wealthy community. He understands 36% of Milwaukie residents are elderly and probably on some kind of fixed income that means their purchasing power goes down. He is not making this recommendation without a great deal of feeling for those facts. Part of trust is that the City has committed to doing everything it can, even in the face of difficulties, to maintain a service level and spend time with those in the community seeking help. We are not the highest paid employees in local government; however, Milwaukie is retaining some very good people. They are not making the top salaries for their positions. He realizes, too, that part of this trust is that he has to look people in the eye and say this increase is needed. He wants to keep the team because he has really good people who could go elsewhere and make more money. He believes they are staying because they get to do some different and exciting things, and this is a good place to work. The payoff is keeping people's morale and keeping service level and response where it is. The city manager's position here is far lower paid than others, but there are things in this community he wants to see happen. This community is a jewel. He asks people to do a lot, and they are responding. He finds it difficult to make this recommendation because he knows what Councilor Loomis is talking about. He feels it is necessary because the return is there, and he needs to recognize it.

**Mayor Bernard** estimated the City probably saved between \$400,000 - \$500,000 with retirements. This recommendation would cost about \$40,000. That is quite a savings. He used his business's waste oil analogy in which he made an investment to save money in the future. Milwaukie has lost a lot of people and has added a tiny portion back to keep those people whose job duties have increased. Before Swanson, Milwaukie had two assistant city managers, and now there are none. The City has made some significant reductions. JoAnn Herrigel, for example, has many jobs, and each day she gets another one. Swanson is doing Michelle Gregory's neighborhood services job now. He wanted to talk about two of Councilor Loomis's comments. The first was citizen's mistrust. Being on Council and having really studied the budget, the levy failure had nothing to do with mistrust. The problem was not being able to communicate with enough people about the need and the value of Milwaukie's services. People who "voted for me" – that is a terrible thing to say. He works for the citizens of

Milwaukie. He was standing on a downtown street corner pulling weeds. A person walked up to him and said he sure wished he could have a City employee weed his yard. Mayor Bernard responded he was not a regular City employee and gets \$200 a month from the citizens. People who vote for him are the citizens of Milwaukie whether they voted for him specifically. He works for the citizens, not the people who vote for him. Swanson refused his 3% last year hoping to communicate to the people how important the levy was. That was a big sacrifice.

**Councilor Loomis** asked where this argument was last night when someone was being laid off.

**Mayor Bernard** said the City Council was adopting a budget, not laying off a person. The work is still there even though people have left the organization. His argument is that the same management is doing a lot more work. The chief, captains, sergeants, and officers will have to pick up the delivery clerk's work.

**Swanson** said he got lucky doing this year's budget because he was able to reduce personnel costs through retirements and resignations. Oftentimes in a freeze, it does not fall the right way. In this case he only had to cut one position. It is no reflection on that person; she is a wonderful person he has known for several years. It is the function. During a harder time, the position is difficult to justify. He could not recommend that function because when times are good it is probably affordable but not in these times. That is the reason that cut was made. Even if this non-represented COLA is not approved, Swanson could still not recommend that function.

**Councilor Loomis** assumed the job was important and did not realize that was a luxury job.

**Swanson** reiterated the action was no reflection on the person; she is wonderful. It is the function.

**Councilor Stone** understands this potential 3% COLA would amount to about \$40,000 and asked how many employees this covered.

**Rowe** said it would cover fewer than 30 management, confidential, and seasonal employees.

**Councilor Stone** asked if these employees received raises other than cost of living.

**Swanson** replied some receive merit increases based on annual evaluations while others have been with the City for a number of years and are no longer eligible for merit increases.

**Councilor Stone** asked how many of these people are peaked out on their salaries.

**Rowe** said most of these employees have reached the top step in their classifications.

**Councilor Stone** said these people are PERS recipients and understands the City is paying significantly more this year for PERS. She recalls it was \$300,000.

**Swanson** believed the original number was \$112,000 or \$250,000 but would have to confirm that.

**Councilor Stone** is sensitive to what Councilor Loomis is saying as well as Mayor Bernard and Councilor Lancaster. We have downsized a little bit like everybody in the public and private sector. We are doing more with less. She thinks public employees are getting pretty well paid, and retirement packages are very good if you look at the entire compensation package. She is not opposed to giving people cost of living increases to keep up with inflation as interest rates fall. She is also sensitive to the fact the City is in a budget crunch. Like Councilor Loomis said, we are seeing positions lost but continue to give increases. They have had increases thus far through PERS and their benefits packages. She is torn about this. On one hand, they are compensated by years of service and several have gotten merit increases as well.

**Swanson** said there are two issues relating to PERS. He was asked about that during the election. One gentleman asked how much the City spent as a total bill for PERS. After doing manual calculations, Swanson got back to this person and told him it would be a lot of money. The City administers PERS; it does not create it. He is close enough to the age of collecting PERS and knows it is a good program. He further knows many expectations, including his own, have been changed because of what is going on in Salem. It had to happen. Thinking back to what he told this gentleman, it is a good program, and he will not argue anything other than that. He also told the gentleman each time he and other employees get up in front of the community, remembering its demographics, they feel the difference. He is working for people who are not wealthy and are on fixed incomes, and he gets a much better retirement than they ever had a chance of getting. He and others who work for this organization understand they do owe people in this community a lot. Swanson does feel gratitude, but at the same time he is competing with other cities that have the same thing. He does not want them to take away some of the people the City employs right now. Milwaukie is in a good position, and it is moving forward. The reason the City is moving forward is twofold. In addition to the regular volunteers like Aschenbrenner, Ball, Michel, Howell, and Zumwalt, the community is supportive. The second reason is the City has people who are willing to translate that into positive action. Swanson desperately wants to keep that momentum going, and this is one way to do it. He knows other city manager positions pay more money, but there are exciting things here to be accomplished.

**Rowe** addressed questions and comments about the total compensation package. The cost to employers for PERS is increasing, but the PERS system is also being restructured. The PERS package at retirement will not be what was anticipated when employees came into the system. It is difficult to give it a dollar amount and what it means to total compensation. The City received notice from PERS yesterday that the rates would be lower than previously identified; however, another new rate will be out in

three months. The City of Milwaukie has the same health insurance package it has had for a number of years, and increased costs are shared between the employee and the employer. City employees at all levels have taken a 5% increase on both medical and dental insurance premium costs. The total compensation picture is not necessarily increasing relative to inflation because of these shared costs in the collective bargaining agreements. Non-represented employees follow those agreements.

**Councilor Lancaster** made a final comment on Councilor Loomis's remarks about trust. Trust is something we can never stop working on. He got into City government 5-1/2 years ago. Where Milwaukie was then and where it is today are two completely different organizations in terms of its relationship with the community and the trust issue. There will always be some level of mistrust, and to a degree nothing can be done about that. What we can do is do the right thing, demonstrate it, and be open and honest with everything at all times. That is where we are now. Councilor Lancaster's sense is compared to five years ago in the recall scenario, the majority of citizens do have trust in this body, and a lot of credibility has been established. By continuing to do what we are doing right now will make it better over time.

It was moved by Mayor Bernard and seconded by Councilor Lancaster to adopt the City of Milwaukie 2003 – 2004 pay table with salary schedules effective July 1, 2003 for non-represented employees. Motion failed 2 – 1 – 1 with the following vote: Mayor Bernard and Councilor Lancaster aye; Councilor Loomis nay; and Councilor Stone abstained.

#### **Authorize the City Manager to Sign Annual Purchase Orders Exceeding \$25,000**

**Councilor Stone** earlier requested this item be pulled from the consent agenda. She understands these are annual contracts and asked how these have been handled in the past.

**Swanson** said typically these are handled the same way each year. He does not have authority to sign these individually, so Council must authorize him to do so. He discussed the types of purchase orders. Some, such as the one with Clackamas County Fire District #1, is an established amount. Others, such as Office Depot, are open purchase orders that can be used, with authorization, for supplies during the fiscal year.

**Councilor Stone** asked if the city manager has a limit on what he can spend.

**Swanson** said his limit is \$25,000.

**Councilor Stone** asked if that is something the Council increases periodically if it sees fit.

**Swanson** said it seems to be working right now and does not anticipate any need to amend the amount at this time.

**Firestone** said his experience has been most jurisdictions have set the amount at \$25,000.

**It was moved by Mayor Bernard and seconded by Councilor Lancaster to adopt the resolution authorizing the city manager to execute certain contracts for fiscal year 2003 – 2004. Motion passed unanimously among the members present.**

**RESOLUTION NO. 30-2003:**

**A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF MILWAUKIE, OREGON, ACTING AS THE LOCAL CONTRACT REVIEW BOARD, AUTHORIZING THE CITY MANAGER TO EXECUTE CERTAIN CONTRACTS FOR FISCAL YEAR 2003 – 2004.**

**Other Discussion Items**

**Mayor Bernard** requested the cost of living adjustment for non-represented employees be on the next agenda when there is a full Council.

**Mayor Bernard** appreciated Councilor Lancaster's comments on the sewer billing and paying down the debt and planning for the future

**Update on Sam Marinos House**

**Councilor Stone** wanted an update from Swanson on the situation with the Sam Marinos house.

**Swanson** reported the demolition started today. The person recycling parts of the house started, and the process should be done by the end of the week. He recapitulated e-mail he sent each of the Council members earlier today. He has had the authority for almost two months to act. In order for the City to effect an abatement on a property to which it does not have access, the code requires the City secure a judicial warrant. The warrant allows, among other things, the City to enter the property. Having drawn this out over a couple of months in order to come up with an agreement, the City has had to go back to the court a number of times and request extensions of the warrant. At some point in time, and appropriately so, the court will probably say, "do not use me any more." The judge could exercise his discretion not to extend the warrant. Without the warrant authority the City to enter the property, he cannot do anything. This was Swanson's judgment and his concern; the City would probably find it difficult to extend the terms of the warrant that expires at the end of this week. He was in a position where he either had to do nothing and basically lose any authority to effect a change on the property, or he had to move. It was a judgment call. It is not appropriate to get a read from the judge prior to applying for something; they do not tend to like to do things like that. He got to the point he believed his authority would effectively end this week, and he would have to sit back and let it happen. He does not believe that would be a good idea. The property is clearly a nuisance under the terms of the code.

He could either sit and do nothing and let his power to make a difference wane, or he had to exercise his authority. He chose to exercise it realizing it was probably not a popular decision with some people. He felt the City was at a point where he questioned whether the nuisance provisions of the code were going to mean anything and whether they would have any force and effect. That was the choice he made.

**Councilor Stone** understood Swanson's dilemma and the warrants to exercise his authority. There has been a lot of testimony to save this structure as recently as last night. She was under the impression there was going to be some dialogue between him and Ogilby. Has there been any dialogue?

**Swanson** talked to Ogilby last week and told him what would need to be done in an ideal situation. Part of that was the Monday deadline. In order to preserve the City's authority to abate, Swanson needed to have the house gone. He did not give Ogilby a lot of hope last week. At this point, it was a judgment. He could proceed with the abatement or take a chance that something could be put together, but he would not have a lot of power to enforce it.

**Councilor Stone** asked if that was only if another warrant was not granted.

**Swanson** said that was correct, but he has no way of predicting if the judge would extend the warrant. In his estimation, it is improper to go to the judge and ask for an extension. Each judicial decision is based on merit, and he would not put a judge in that position because he feels it is not proper use of resources. He respects the court too much. It was his call.

**Councilor Stone** understands this is Swanson's call. This is an extenuating circumstance, and she does not know if the judge knows all the ins and outs of this. She said it last night and will say it again -- she really believes the Council needs to live by the words of the mission statement and the community goals. Demolition is in direct conflict with both of those things. We are not preserving our built environment. We are not living up to saving structures that are either historically or architecturally significant. We had a lot of people testify at one of the May Council meetings. A lot of people came forth. The greater majority of them, she counted approximately 20 different pieces of testimony, were for saving the house. We have yet one more person stepping up to the plate, and he seems to be a very credible, professional fellow. She read through the material he presented to Council last night, and the City probably does not have another choice. Because we have a batter stepping up to the plate and ready to swing, she believes the City needs to take that risk and say, "isn't this a piece of our history worth preserving? Isn't this a structure that could potentially be someone's home?" It has a history. It is part of our past, and she really feels the City should look at that. This is Milwaukie's centennial year. She knows there are a lot of things that would make everybody probably on this Council agree the structure should be saved. We have gotten ourselves into a real tight corner. She really thinks the City Council has a choice. She has no reason to believe Mr. Ogilby would not move the house. He has moved the Frank Lloyd Wright house to Silverton. He has moved several houses recently including

an historical home near 39<sup>th</sup> and Hawthorne. He can do it. She would at least like to see some talk happen between Swanson, Ogilby, and the demolition contractor, Mr. Obrist, before this takes place. It may change Swanson's decision.

**Swanson** knew this would put him in direct conflict with some of his bosses. The City's preservation report card cannot be created on just this one structure. The report card has to be written with a look at what has been done overall. As an organization, the City has lived up to its mission statement and community goals because, again, one structure cannot determine pass or fail. We may have failed to do it on the structure but on the system as a whole, he believes there is evidence of the City's having done a pretty good job. His decision to go ahead with the demolition is not a comment on this particular contractor. It is merely a realization we are at a certain stage in the process. He started the nuisance process because he believed there was a nuisance. If he were to let it wither away and die, which would have been the effect, then he did not make a very considered judgment when the petition was originally filed. It is not a comment on this gentleman. This thing has had a history. There are people who want to save the house and have expended energy toward the deadlines, but the energy has not been consistent over these two years. The City issued a request for proposals (RFP) that would have allowed Ogilby to come in and take the house. There were opportunities. The history has been there is always one more chance, one more answer at the eleventh hour. In some ways the question that should be asked of him is, "what have you been doing?" He believes it is more a comment of where we find ourselves in the process. He felt the choice was to either move ahead with the abatement or forget the nuisance. He feels that is what it has come down to and admits part of it is a judgment on his part.

**Councilor Stone** asked a logistical question. If the warrant did not end on Friday but in two weeks, would Swanson be more apt to talk to the preservationist who wants to move the home? Might he feel more comfortable about the end result? She senses a lot of his decision is because of the time deadline of the warrant expiring on Friday. She asked if she was correct in sensing that.

**Swanson** said that, in part, was correct. He also suggested making sure people understand that the timeline exists not because we have not been diligent in trying to solve the problem. If we have come to this place and find ourselves in a time crunch and review what has gone on over the past year, again, he thinks one would find very little activity until there is a pressure point. Then everyone gets moving right away.

**Councilor Stone** wanted to speak to that comment. In reference to the RFP that went out initially when the house was still owned by the School District, Swanson speaks of "the person." She assumes he means a member of the Wisner family or the people who are really trying to save the house now. In the work session, it was stated they did not have the means to move the house, but they were involved. They actually campaigned at that point, because she recalls the School District was going to demolish it. The house has seen the ball and chain coming before, so the family was very active. When Peterson took it, the activity stopped because the family thought it was in good

hands. Then it revs up when Emmert takes it and goes down because they think it is in really good hands because Emmert is internationally known. She does not want people to think that the parties interested in saving this house had done nothing. She thinks we are being a little bit negligent, too, as a City. The goal is to try to save this house, and she thinks everyone on Council wanted to see that happen. She could be wrong but believes she has heard that from at least most of the Council people. She thinks the Council is being negligent if it does not consider this third batter up to move the home. He really wants to move it, and he has the means and track record to do it. In terms of this being characterized as this being just one house, it is not just one house. Milwaukie has lost several houses over the years. In January of this year, there was a presentation by Patty Wisner that alluded to that. She gave the Council a whole packet showing all the homes in Milwaukie that have been destroyed or moved. This is not the only one. It feels to her like we are just letting pieces of our history leave us either by being floated down the river or being demolished. At some point, it has to stop. We hardly have anything left.

**Mayor Bernard** requested Councilor Stone to stop because demolition has already started. According to what he has been told, when it is time to take the windows out, the contractor takes a saw and cuts them out. At that point the structure is no longer sound. If she drives by, she would see that.

**Councilor Stone** said she was not through making her comments and would appreciate as a member of this Council being allowed the time to do that.

**Mayor Bernard** appreciated that but was concerned Council is wasting its time because he understands demolition has begun. It is too late. The City has a contract for which it is responsible for upholding.

**Councilor Stone** said she had one more question for Swanson. In terms of what has been done, she understood him to say the people who take things out of homes have completed the interior work.

**Swanson** believes that is correct and understands the window removal has been started. The contractor has made some progress today.

**Councilor Stone** asked it was truly not possible to stop this. She is an eternal optimist, and it "ain't over 'til the fat lady sings." She thinks the City is making a mistake. The Council has heard from a lot of citizens who want to see this house preserved. It is not just one or two people. It is a piece of our history. She has no reason to believe Ogilby will not follow through. It is a gamble, and one would have to be willing to take it. Swanson is obviously not.

**Swanson** said he has been gambling for the last two months with authority that he received on May 7. The decision he made is to exercise his responsibility. He has spent two months throwing the dice, and now is the time to stop. Councilor Stone is correct. He made a decision not to gamble at this point in time, but he made it because

he felt he had a track record of two months, and probably more, of gambling. He feels personally he is among the people who want to see the house saved. He has given a great deal of effort over the past couple of months to try and make that happen. At some point he also has to look at maintaining the integrity of the code, the nuisance provisions, and the decision that was originally made which would basically, in his judgment, disappear at the end of this week. He thinks it is improper, but someone could talk to the judge and ask him if he would extend the warrant. Maybe he would say yes. In his judgment, he does not believe that is something that should be pushed again. Once again, this is not a comment on the person who wants to move the house. It is merely a comment on finally getting to the point where he felt he had to take some action. He personally feels comfortable with his decision and that he did everything he could up to that point. He feels the answer he came up with is appropriate.

**Councilor Stone** had questions about legal matters regarding the I-beams supporting the house and that there may be some problems about damaging that equipment belonging to someone else if the house is demolished.

**Firestone** understands the contract with the demolition contractor made it clear certain things belong to a third party and are to be preserved.

**Councilor Stone** had heard the owner of those pieces of equipment was concerned and was looking into it legally.

**Firestone** said it was his understanding there had been direct contact with the demolition contractor.

**Councilor Stone** is not happy with the decision, and it is sad a piece of history will be destroyed once again. She does not think it reflects well on the Council and the City because the mission statement and community goals are not being upheld. It does not make her proud at this moment to be sitting on this Council to know this is going to happen. She asked Swanson if he was given the information Ogilby provided at last night's meeting.

**Swanson** said he had.

**Councilor Stone** understood Swanson had chosen not to call Ogilby because he had made his decision before.

**Swanson** talked to Ogilby last week and basically informed him this would be the outcome. He informed Ogilby as he was driving from Rhode Island to Massachusetts in a phone conversation that he would be exercising his responsibility to proceed with the abatement if the house were not moved by Monday. If Ogilby is suggesting anything else, then Swanson will reverse his former statement. He and Ogilby had a conversation between 3:00 p.m. and 4:00 p.m. EDT. Swanson said he would produce his cell phone records. Ogilby at that time was told the chances were probably not great because he had already committed that Monday was the drop-dead date.

Monday was also the drop-dead date that was set in a conversation he had with Patty Wisner on that Monday as he was proceeding from one spot in Florida to another to visit relatives. The request was made for him to hold off for another week because a contact had been made with Mr. Emmert about an option that would have him take off the top of the building and move it within the week. He said fine and that he would hold off to Monday, June 30. He stated that if it was not removed by that date, he would proceed. They may not have heard that today, but they heard it on Monday and Tuesday of last week. He knew at that point in time that his time was running out. He actually extended the time to make the last Emmert option work.

**Mayor Bernard** said the City Council voted 4 – 1 to support the city manager's decision at the June 10 meeting. He felt the City Council needed to stand by that. The decision has been made. He thought the City has been gambling for about 2-1/2 years hoping to save the house. Currently, the City does not know who owns the property. There is no title. It is personal property that has been abandoned on a piece of land with no ownership assured anywhere. That is part of the big problem. Who do you talk to about taking it over when no one claims it?

**Councilor Stone** asked if there was a determination on who is the rightful owner of the house.

**Firestone** said at one time it was Mr. Peterson. It depends on how one reads the agreement between Mr. Peterson and Emmert International. He has not seen the agreement and would not hazard a guess as to who owns it. If Mr. Peterson is the owner, he certainly has abandoned the house. If the owner is Emmert International, the company has had plenty of opportunity.

**Councilor Loomis** is disappointed the house is going to be destroyed, but he supports Swanson. The thing that really bothers him is that the City has really stepped up and tried to save the structure, and in the end some will feel the City is responsible for its destruction.

**Councilor Stone** agreed with Councilor Loomis. She would not have a problem throwing in the towel and saying the City has done all it can. Now there is a third batter at the plate, and the third time is a charm. He should be given a chance, but the City is not doing that. She understands Swanson's position completely, but she thinks it is worth taking the risk. It is worth taking the gamble to see the house moved and not demolished.

**Mayor Bernard** announced the City Council would meet in executive session immediately following adjournment of the regular session to discuss real property transactions pursuant to ORS 192.660 (h).

## **ADJOURNMENT**

**It was moved by Councilor Lancaster and seconded by Councilor Loomis to adjourn the meeting. Motion passed unanimously among the members present.**

**Mayor Bernard adjourned the meeting at 8:30 p.m.**

Pat DuVal  
Pat DuVal, Recorder



# Memorandum

**To:** Jay Ostlund, City of Milwaukie

**Date:** June 13, 2003

**From:** Jeanette Hahn, Bryan Kean, and Ed Cebron, FCS Group

**RE** Sewer Rate Update for Fiscal Year 2003/2004

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## Background and Scope of Work

In 2001, FCS Group performed a sewer rate study for the City of Milwaukie that included recommendations for changing to a volume-based billing structure. As a result of that study's recommendations, the City adopted a 3-year graduated implementation, during which the fixed charges decreased as greater reliance on volume-based rate revenue was phased in. During each of these annual rate structure changes, a small increase was also built into the structure to ensure that the utility continued to collect revenues sufficient to cover full operating, capital, and policy-related costs and obligations.

For fiscal year 2003/2004, the City was scheduled to implement its final rate step, in which the fixed portion of the rate dropped to \$15.00 per unit (from \$22.00), and the volume charge increased to \$2.10 per hundred cubic feet (ccf) for residential and \$2.95 per ccf for commercial (from \$1.40 and \$2.75). This final step also included a roughly 4.5% increase in annual rate revenues, based on needs projected in the 2001 study.

During the past fiscal year, the City has become concerned that revenues are exceeding the rate study's original projections and that customer volumes may be higher than originally estimated, with the result being excess revenue generation. In the fall of 2002, FCS Group assisted the City with an audit of the billing system to ensure that the software was accurately calculating and imposing the sewer rates as intended. That audit found that there appeared to be no malfunction of the billing system, but that indeed, residential volumes billed exceeded those used to design the adopted rate structure, generating roughly \$200,000 in revenue in excess of original rate study projections. At this time, there is no explanation available as to why residential volumes are higher than history available at the time current rates were designed, but it can be assumed that the billing software itself is implementing the rate structuring properly.

In June 2003, the City hired FCS Group to conduct an update to the sewer rate study, as a follow-up to the volume-based sewer rate implementation conducted for the City in 2001. Our scope of work for this update included reviewing and validating current and budgeted financial and customer data provided by the City, forecasting rate revenue requirements based on updated operating and capital needs, restructuring sewer rates as needed to continue policy goals developed in 2001 and recover sufficient revenues, and recommend an updated strategy for the utility as it enters the 2003/2004 fiscal year.

## Data Sources and Key Assumptions

Data for the analysis was provided by the City and included monthly revenue collections and volume reports across customer classes, sewer fund balances projected at the beginning of the upcoming fiscal year, proposed budget for the upcoming fiscal year, and the capital improvement program (CIP).

The data was used to update the 2001 rate model, including revenues by customer class, revenue requirements, CIP funding analysis, and key assumptions that drive future forecasts in the model. While the model is largely unchanged structurally, there were several assumptive changes made:

- o Interest earnings rate was reduced to 2%, reflective of current economic conditions.
- o Customer growth was reduced to 0.05% -- the level necessary to match to current SDC collections.
- o Debt interest rates were reduced to 4%, reflecting the current market.
- o Inflation was left at 3%. Given the interest earnings assumption of 2%, this is a conservative choice.
- o Customer consumption volumes, as reported during the twelve months between May 2002 and April 2003, were projected to remain the same in coming years, adjusted only for growth.
- o Assessments and loan payments tied to assessments were set to zero, reflecting the budget.

The revenue requirements forecast projects utility needs through fiscal year 2007/2008, based on the City's fiscal year 2003/2004 budget, escalated by inflationary factors. Several line items in the budget were altered for future years, based on discussion with City staff, in order to generate a realistic picture of future needs. (The detailed forecast is included as an attachment to this memo.)

## Revenue Sufficiency Test Results

There are three categories of obligations we examine in our rate revenue requirement analysis:

- o Capital program funding,
- o Ongoing operating, maintenance, and administrative expenditures, and
- o Policy requirements.

*Capital Program Funding:* In its current CIP for 2003/2004 to 2007/2008, the City has identified \$1.7 million in needed infrastructure improvements. Our forecast indicates that all of those needs can be met by existing and future cash reserves, with the utility still maintaining a healthy reserve at the end of the forecast period (roughly \$4.2 million by 2008). At present time and throughout the forecast, the sewer utility has no debt repayment obligations. It should be noted that the utility will be undertaking a master planning effort in the near future, which will likely identify additional capital projects; the results of that new CIP will change this forecast.

*Ongoing Operating Expenditures:* For fiscal year 2003/2004, the City anticipates total operating expenditures of \$2.77 million. Based on projected rate revenues for the end of fiscal year 2002/2003 and assuming minor growth, we can anticipate \$2.81 million in rate revenues for the upcoming fiscal year. Thus, in the upcoming budget year, rate revenues are able to cover total operating costs. By the end of the analytical forecast period, we project that, without inflationary-level rate increases, costs will outstrip rate revenues. Throughout the forecast period, the utility is able to sustain its minimum working capital of 45 days of annual operating expenses (roughly \$350,000).

*Policy Requirements:* Finally, as described during the 2001 rate study, it is the City's policy to generate cash from rates on an annual basis to be used strictly for capital reinvestment in system infrastructure. That amount is linked to the utility's annual depreciation expense, which is nearly \$150,000 per year. This policy continues to be prudent fiscal management, giving the utility the capability to cash-fund capital improvements and demonstrate willingness and ability to repair, replace, and maintain capital facilities in a systematic, proactive fashion.

After assessing the sewer utility's ability to fund its currently identified CIP, existing levels of ongoing operating expenses, and policy of annually generating cash to reserve for future capital needs, our test of cash flow sufficiency indicates a need for moderate, inflationary-level rate increases over the next several years. Given the City's concerns about perceived "over collection" of rate revenue during the past year, we recommend that the utility forego the previously adopted 4.5% rate increase that was to become effective July 1, 2003. The implication of this decision is that, if operating costs are incurred as budgeted, the utility will not be able to fully fund its depreciation expense and dedicate it for future capital. (A little less than half that policy can be funded with no increase.) As mentioned, though, projected rate revenues for 2003/2004 exceed budgeted operating costs.

In subsequent years beginning with fiscal year 2004/2005, we find that annual rate increases on the order of 2% to 3% are needed to meet rising operating costs and the capital funding policy. To the extent budgeted expense inflation is lower, required rate increases will be a lower; conversely, if there is a future increase in the level of service (e.g., new personnel, higher level of maintenance, etc.) not implicit in the 2003/2004 budget, these rate increase may not be sufficient to cover those programs.

These projected increases after the upcoming fiscal year are stable and consistent with the projected 3% inflation rate. Given the funds available in the construction fund and the moderate CIP, this is a reasonable and expected result from the rate analysis. In comparison to the original projections from the 2001 study, actual revenues received are higher, but so too are expenses.

## **Rate Structure**

While we are not recommending a rate increase for fiscal year 2003/2004, we believe the City should continue the phased-in restructuring of the actual rate structure, started in 2001. That approach ultimately targets a \$15.00 monthly fixed charge, versus the current \$22.00 charge, completing the conversion to a reasonable volume-based pricing structure.

However, because we're recommending that no additional rate increase be implemented while completing this restructuring, we needed to recompute the appropriate volume rates to accompany that \$15.00 fixed charge. Volume rates were computed to generate the same amount of revenue by class as the current rate structure. Under the rate structure displayed in the following table, the City will generate 59% of revenues from volume charges from the residential class, as opposed to 41% in the current structure. (In the commercial class, 96% of revenues are derived from the volume charges, versus 93% in the current structure.)

### **Recommended 2003/2004 Monthly Sewer Rates**

<i>Customer Class</i>	<i>Fixed Rate per Month</i>	<i>Volume Rate per ccf</i>
Residential (Including Multi-Family)	\$15.00 per unit	\$1.96
Low-Income Residential	\$7.50 per unit	\$0.98
Commercial	\$15.00 per account	\$2.93

These rates are based on statistics taken directly from or derived from utility billing reports for the 12 months ending April 2003. Because no reports are available which show actual units billed (i.e., only the number of accounts were available), we derived the number billable residential units based on revenues received.

It is important to recognize that while these rates should result in a revenue neutral position for the utility as a whole (roughly \$2.81 million), individual customers will see changes in their bills, either an increase or a decrease from current rates, depending on their volumes. Customers with volumes lower than average will see a decrease to their bill, while customers with above average volumes will pay increased sewer bills.

### **Recommendations**

Our recommended action plan focuses on three areas: rate revenues needed, rate structure, and future financial planning.

*Rate Revenues:* We recommend that the City sustain rate revenues at current levels for the 2003/2004 fiscal year. Projected rate revenues currently exceed budgeted operating expenses; though, without a rate increase in the upcoming fiscal year, the utility will not be able to fully fund depreciation as a cash contribution to its capital reserves. Nonetheless, with concerns about revenues realized at levels higher than originally projected and healthy fund balances on-hand, it is reasonable for the City to forego the previously adopted 4.5% rate increase for the coming fiscal year. In subsequent years, we project annually inflationary-level rate increases needed to fully fund operations and policy requirements. Should the City identify additional levels of service required in operations and maintenance or capital, it may need to revisit this forecast of rate increases.

*Rate Structure:* We recommend that the City continue to modify the sewer rate structure to lower the fixed charge to \$15.00 from the current \$22.00 rate. This step completes the transition to the volume-based rate structure approved by the City Council in 2001. We have recomputed the

appropriate volume rates to accompany that charge yet sustain rate revenues and existing, projected levels. (The recommended rates are displayed in the above table.)

*Future Financial Planning:* Given the utility's healthy reserves throughout the forecast period, we recommend that utility management identify needs for those reserves as it continues and plans its capital program. It is our understanding that the utility will be preparing a master plan in the coming year, which will inevitably identify needs which can be funded at least partially by cash on-hand. It should be noted that the utility's existing reserves are not excessive, in light of continued capital investments that will need to be made to the system.

It has been a pleasure assisting the City with this update. We look forward to supporting staff in presenting these findings at the City Council's July 1<sup>st</sup> meeting. Please contact us at (425) 867-1802 with any questions or comments regarding these findings.

*(Analytical exhibits are attached.)*

# MEMORANDUM

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TO: Jay Ostlund, P.E.  
City of Milwaukie

FROM: Jeanette Hahn, Project Manager  
Ed Cebron, Principal  
FCS Group, Inc.

DATE: December 18, 2002

SUBJECT: Sewer Rate/Billing Review – Conclusions

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The purpose of this memo is to describe the conclusions of our summary-level audit of sewer rates and billing data for the City of Milwaukie. The evaluation was requested to identify the potential cause for a discrepancy between projected and actual sewer rate revenue coinciding with the implementation of volume-based sewer rates.

This evaluation covered two areas to isolate the potential cause:

- The application of sewer rates within the utility billing software and
- The consistency of actual customer data versus statistics used to compute the rates in the original analysis.

**UTILITY BILLING SYSTEM** – The City provided a set of actual bills sent to customers in different classes for FCS Group to validate that the sewer rates were being applied correctly within the billing software. Of the six sample bills provided, all of them were computing sewer charges correctly. At this time, there is no reason to suspect that the billing system is inappropriately charging for sewer.

While the six sample bills were selected due to customer complaints and abnormal usage patterns, sewer rates applied are accurate. In most of the cases where individuals complained about high bills, their measured winter average consumption (December through March) was well above the estimated residential winter average of 13 ccf bimonthly per living unit.

Most notably, in the sample bill for Account 002939-000, the customer's reported winter average was 21 ccf, 8 ccf above the class average. Interestingly, December proved to be the month with the highest consumption for that customer all year, with 26 ccf of water used. The next highest water consumption posted was in August, with 21 ccf. Clearly, this is an unusual pattern and manifests itself noticeably in the sewer bill. Such anomalies can be caused by a slow leak or a large amount of household visitors during holidays. From a customer service standpoint, it may be worth following up on cases like this with the customer directly. Outside of a leak adjustment or some extraordinary circumstance, the sewer rates are nonetheless a valid representation of the costs incurred to serve that customer.

Account 16-2660-00's August-September bill is another case of an extraordinarily high sample bill that resulted in a customer complaint. In this case, however, despite the customer's complaint, it is clear that the sewer bill is not the culprit. The customer is being charged for a winter average consumption of 14 ccf bimonthly, comparable to the class average. However, the customer does have a history going back to 1996 of having water bills in the September-October period nearly double those from other bimonthly periods.

It appears that many of these individual complaints are the result of "sticker-shock." These customers have posted water consumption outside the norm for their class, and the intent of volume-based sewer rates is to shift cost recovery burdens to customers in proportion to their use of the utility system. Higher volumes yield higher costs of providing service. Under a fixed rate structure, these higher volume customers were subsidized by low-volume users. Nonetheless, it may be worthwhile to follow-up with customers, such as Account 002939-000 where the consumption pattern is truly unique, to see if there is a valid problem to correct.

**CUSTOMER DATA CONSISTENCY** – The City provided general billing reports for each billing cycle from July 2001 through October 2002, identifying the number of accounts billed and the amount of volume billed in each cycle. Extrapolating from revenue figures, City staff also identified the average number of living units billed, for purposes of checking revenues from the fixed charge.

Using this information, FCS Group compared the actual totals to the underlying data sets used to compute the sewer rates in the 2001 study. It is this test that identified the potential cause of the revenue discrepancy the City is experiencing.

In the rate study, detailed customer data was collected to use as the basis for allocating annual utility costs to customers and deriving rate components to recover those costs. The customer data used was based on year 2000 information and projected forward for 2002/2003 cost recovery. FCS Group worked with the City's information systems consultant to extract this data from the billing system, and after two iterations, a database of raw customer data was found that reconciled to actual rate revenues collected during the same period, within an acceptable margin of error.

Despite these checks, it appears the City's recent experience has deviated from the projected volume data generated through that study process. If the rate structure is based on a data set that is lower than actual performance, the rates themselves will over-collect the annual revenue need. Conversely, if the underlying data set is higher than actual performance, the rates will under-collect expected revenue.

The information in Table 1 compares the statistics from the raw databases used to generate rate structures during the study against data pulled from the City's summary reports. The key discrepancy exists with the volume data; the information used to set the rates appears to be lower than the volumes actually being billed. This means that the rate structure collects more revenue than is needed to meet the identified annual need by an estimated \$17,000 per month or roughly 7% per year, when priced out at the prevailing rates.

**Table 1. Data Comparison and Estimated Revenue Impacts**

<b>Rate Component</b>	<b>Study Projections</b>	<b>Actual Performance</b>	<b>Difference (Actual – Study)</b>	<b>Estimated Annual Revenue Impact</b>
Units/Accounts Billed	9,437	9,374	(63)	\$(8,250)
Volume Billed (ccf):				
Residential	656,372	755,802	99,430	\$139,202
Commercial	195,178	222,524	27,346	\$75,202
<b>Estimated Total Revenue Impact from Projections:</b>				
<b>Annual Over-Collection (Under-Collection)</b>				<b>\$206,154</b>
<b>Monthly Over Collection (Under-Collection)</b>				<b>\$17,179</b>

**RECOMMENDED COURSE OF ACTION** – Before altering the rates to account for the discrepancy, we recommend that the City review its billing data at the detailed account-by-account level once again, in the same manner utilized during the rate study. While an array of sample customer bills was reviewed as a part of this brief evaluation, which all seemed to be computing correctly, anomalies in the individual consumption records themselves could exist that would not be apparent in a small sampling of bills. Indeed, the 2000 database used to set the rates in 2001 did price-out closely to actual revenues reported during the historical period, which suggests it was a valid set of statistics at the time.

However, reviewing customer statistics at the individual account level is a prudent step at this juncture and can be a beneficial part of the complete transition to volume-based sewer rates. Table 2 shows a report format that would be ideal in conducting this detailed exercise. More direction on how to evaluate the account-level statistics can be provided, if the City chooses to perform the task in-house.

**Table 2. Data Report Format Ideal for Evaluating Sewer Account Information**

Acct #	Class	# Units	Metered Water Consumption (ccf)					
			Jul-Aug	Sep-Oct	Nov-Dec	Jan-Feb	Mar-Apr	May-Jun
1234-56	Single	1	16	17	15	12	15	16
<i>(Repeat for all accounts)</i>								

The City has one final step in fully converting its sewer rate structure, to become effective July 1, 2003. That final step places even more of the revenue need in the volume charges; therefore, the first two quarters of the year would be an opportune time to validate the underlying customer consumption records and make any necessary adjustments as a part of that final rate implementation in July. That rate adjustment includes the last of a series of revenue increases (4.5%) that may possibly be foregone, if the detailed data proves to be valid and the over-collection is permanent. If not, it is nonetheless apparent that the 2003/2004 planned sewer rates

may need to be recalibrated to take into account actual, versus projected, customer usage patterns.

Please contact us at (425) 867-1802 with any questions.

# ATTACHMENT F

WS. 2 51



**To:** Mayor and City Council

**Through:** Mike Swanson, City Manager  
Scott Burgess, Community Development Director Pro-Tem  
Dennis Lively, Engineering Director

**From:** Jack R. Ostlund Jr., Associate Engineer

**Subject:** Volume Based Sewer Rate

**Date:** September 11, 2001 for October 2, 2001 City Council Meeting

## **Action Requested**

Adopt the attached resolution for the adoption of the elements of sanitary sewer consumption based rates.

## **Background**

At the Council's direction on September 4, 2001 council meeting, Council adopted a volume based sanitary sewer rate structure. This structure partially charges customers based upon their volume of sewage discharged. Staff is working towards details of implementing this adopted structure.

## **Discussion**

Staff is currently working on implementation issues for this rate structure. Staff requests a January 1, 2002 implementation date for this rate structure. We feel that three to four months will be necessary to test software, hire staff, and dissect scenarios in the transfer to the new structure.

The City currently has a number of customers that have unique situations and have circumstance that make the billing process difficult under standard operations. These cases are as follows:

## **Customers with No Water Usage Data (New Accounts/Change in Accounts/No Data)**

Issue: There are four types of customer that could be affected by this issue:

- New Accounts,
- Changes in Accounts,
- Non-City Water Customers (Well-users, Non-City Customers such as Clackamas River Water District, Oak Lodge Water District, and City of Portland Water users),

These three types of customers are characterized by an absence of data. For these customers we recommend the City charge them the customer-class system average (14 CCF). Staff recommends re-visiting this decision in two years to re-evaluate the equity of this decision.

- Zero Usage Customers.

Unlike new, change in accounts, and well-users, existing customers with zero usage during the winter months do have a usage history. They were part of the system but have a "Winter Average" that is not indicative of their average wastewater discharge. For a variety of possible reasons, the customers did not occupy their homes during the defined winter period and have no sewer usage. The rest of this paper will focus on the policy alternatives the City can implement to define a "Winter Average" for these customers.

When volume-based rates are implemented zero-usage customers present a problem because the billing system for wastewater service would be based on each customer's previous year winter usage. Since these customers have a "Winter Average" that is not indicative of their sewer wastewater usage, we must explore other alternatives for estimating or obtaining average wastewater use. The alternatives for billing customers with no "Winter Average" history are listed below.

### **Alternatives**

- Base the charge on the system-wide average:
- Base the charge on a minimal lifeline charge such as two hundred cubic feet (CCF) for a single-family customer
- Only charge customers the fixed charge.

### **Analysis**

The first option would be to base the charge on a system-wide average is simple to calculate and administer. This method does not give customers who vacation during the winter months a discount for their absence nor does it significantly overcharge

customers who do not establish a "winter average". Customers with zero winter usage or no "Winter Average" history will be charged a rate consistent with their expected use, although individual customers may be overcharged or undercharged.

The second option would be to charge customers a minimum lifeline usage amount such as four CCF for a bimonthly period. This would prevent most customers from being overcharged. At the same time this would also prevent customers from "manufacturing" a "Winter Average" by leaving a slight drip or asking neighbors to turn on outside taps or occasionally flush a toilet. In opposition, this method may not fully account for the usage of customers, at 75 gallons per day.

The third option would be to charge all zero-usage and no-history customers only the minimum charge. This method would assume their discharge is zero until an average is established. In a few cases such as customers who leave during the winter months, the "winter average" may never be established. This method will never fully account for the usage of such customers.

Due to the large number of customers in the City with zero-volume usage during the winter months or no volume history, there would be an impact on the rates based on the policy that the City chooses to adopt that might effect the neutral revenue target.

### **Recommendation**

Any of the options are viable based on the philosophy and direction the City wishes to take. Staff recommends using *Option Two*, upon our experience these residents typically are senior citizens with low usages.

#### **• Customers with no flat fee charge during non-residing months**

Currently customers that do not reside at their residence for part of the year and, have their water service "closed", do not have to pay any bill to the city for services. The current system is made up of both a flat and variable fee. The flat fee is meant to recover the cost of maintenance, repair, and replacement of the cities collection system. The variable fee recovers the cost of treating the wastewater that is produced. Staff recommends that all customers should have to pay, as a minimum, the flat rate in all months of the calendar year. This would be to recover and share the costs, other than treatment, of maintaining the collection system.

### **Fiscal Impact**

This change would more equitably recover the cost of maintenance, repair, and replacement of sanitary sewer infrastructure.

### **Work Load Impacts**

The change would have little effect in the work load of staff.

### **Alternatives**

1. Adopt the recommended charge of flat fee payment
2. Keep the existing rate structure

### **Recommendation**

Staff recommends using alternative 1, minimum charge would be that to support infrastructure maintenance, repair, and replacement.

- **Hiring a ½ time employee to for rate structure**

As was mentioned in the adoption memos, it will be necessary to hire a ½ time employee to aid in the implementation and maintenance of the new rate structure.

### **Fiscal Impact**

The estimated cost of adding an additional ½ time employee is \$20,000 a year (salary and benefits). This cost is built into the adopted rates.

### **Work Load Impacts**

Hiring of ½ time employee is necessary.

### **Recommendation**

Authorize city financial staff to hire an additional ½ time employee

**CITY OF MILWAUKIE  
CITY COUNCIL MEETING  
SEPTEMBER 4, 2001**

**CALL TO ORDER**

The 1869<sup>th</sup> meeting of the Milwaukie City Council was called to order by Mayor Bernard at 6:05 p.m. in the City Hall Council Chambers. The following Councilors were present:

Larry Lancaster

Jeff Marshall

Staff present:

Mike Swanson,  
City Manager

Tim Ramis,  
City Attorney

Alice Rouyer,  
Planning Director

Michelle Gregory,  
Neighborhood Services Manager

Dennis Lively,  
City Engineer

Jack Ostlund,  
Associate Engineer

Jim Colt,  
Police Captain

**PLEDGE OF ALLEGIANCE**

**PROCLAMATIONS, COMMENDATIONS, SPECIAL REPORTS, AND AWARD**

**Mayor Bernard** read a proclamation recognizing the month of September 2001 as *National Alcohol and Drug Addiction Recovery Month*.

**CONSENT AGENDA**

**Mayor Bernard** read the list of consent agenda items:

- A. City Council Minutes of August 20 & 21, 2001;**
- B. Resolution 26-2001 to Amend the City's Current Contract for the Juvenile Diversion Panel;**
- C. Resolution 27-2001 Amending Resolution 17-2001 Setting Fees for Services; and**
- D. Resolution 28-2001 Granting Consent to Clackamas County to Administer Dog Control and Licensing.**

It was moved by Councilor Marshall and seconded by Councilor Lancaster to adopt the consent agenda. Motion passed unanimously among the members present.

**AUDIENCE PARTICIPATION**

None.

## **PUBLIC HEARING**

### **Volume Based Sewer Rate**

**Mayor Bernard** called the public hearing on the proposed sanitary sewer rate charge to order at 6:09 p.m.

The purpose of this hearing was to consider public comment on the proposed volume based sewer charges.

Staff Report: **Ostlund** introduced Ed Cebon, Financial Consulting Solutions Group, Inc. (FCSG), consultant who worked with the Citizens Utility Advisory Board (CUAB) and staff on the proposed rate structure.

**Cebon** reviewed the background of the volume based rate structure. After adopting a sewer rate increase in February 2000, Council directed staff to determine if a volume based structure would be more equitable than the flat rate method. After reviewing policy and technical options with the CUAB, several key issues were identified: conservation should be encouraged and rewarded, billing based on residential customer winter usage is appropriate, and transition to a new structure should be phased in over 3 years. In addition to charging a more equitable fee, proposed charge is intended to create financial stability for the utility.

The CUAB considered patterns of customer usage and recommended the 3-year program with gradual increases. Customers will have the opportunity to evaluate their conservation options during that time. The impact on City revenues is neutral and is not intended to create untoward increases.

**Councilor Marshall** was concerned about accounting for administrative costs, including consumer education, related to implementing the new rate structure.

**Cebon** said additional funds, generated while customers adapt, can be used for additional administrative expenses. There will be certain start up costs related to researching customer records and developing administrative procedures.

**Councilor Lancaster** understood this was a very complex issue and would be concerned if rate increases were needed to support rising administrative costs. He asked if the impact of zero-volume usage had been determined.

**Cebon** said impact would be slight since research shows there are actually very few zero-volume customers. Those on wells will be locked into the system average until such time as they connect to the municipal system.

The group discussed the low-income residential rate, and **Cebon** believed applications were approved based on Clackamas County standards. There are currently about 100 low income customers.

**Councilor Lancaster** noted this is a pay-as-you-go program and all fractions are rounded down when bills are calculated.

Correspondence: None.

Public Testimony: None.

**Carla Bantz**, 4439 SE Pennywood Drive, Milwaukie, spoke in opposition to the increase. She believed the proposed rate structure would place a burden on families, and seniors would not see the rate decrease they anticipated. She was concerned additional residents would have their water shut off each month.

**Sara**, 6136 SE Monroe, Milwaukie, was opposed to the rate structure. Families with children would have high utility bills. She did not feel the public information accurately stated the percentage of increases.

**Lee Cox**, 11656 SE 48<sup>th</sup> Avenue, Milwaukie, supported the volume based rate structure. She believes the current flat rate subsidizes large families with high water consumption.

**Councilor Lancaster** felt the volume based rate proposal was the best compromise and discussed rising treatment costs.

Staff Comments: None.

Close Public Hearing: **Mayor Bernard** closed the public testimony portion of the hearing at 6:45 p.m.

Council Decision:

**Councilor Marshall** agreed volume based method seems to be the best compromise and is perceived as being overall the most equitable. It encourages the option to conserve. He suggested residents write the Clackamas County Board of Commissioners and urge construction of a new, more efficient treatment plant to replace Kellogg.

**Councilor Lancaster** said the Council will remain open to other community suggestions as the 3-year program is implemented.

**It was moved by Councilor Lancaster and seconded by Councilor Marshall to adopt the resolution establishing sewer service charges. Motion passed unanimously among the members present.**

**RESOLUTION NO. 29-2001:**

**A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF  
MILWAUKIE, OREGON, ESTABLISHING SEWER SERVICE CHARGES.**

**OTHER BUSINESS**

**Recommendation to South Corridor Policy Group**

**It was moved by Councilor Marshall and seconded by Councilor Lancaster to forward the Milwaukie City Council recommended options to the South Corridor Policy Group for further study. Motion passed unanimously among the members present.**

**Other**

**Councilor Marshall** expressed his concern with flaglot language in the Comprehensive Plan and suggested the Planning Commission review it.

**Rouyer** said the Planning Commission is scheduled to discuss flaglot standards at its September 25 meeting.

**Mayor Bernard** announced the City Council discussed updating the Community Goals at its September 1 work session and will meet with staff to discuss action plans.

**ADJOURNMENT**

**It was moved by Councilor Marshall and seconded by Councilor Lancaster to adjourn the meeting. Motion passed unanimously among the members present.**

**Mayor Bernard** adjourned the meeting at 6:50 p.m.

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Pat DuVal, Recorder



**To: Mayor and City Council**

**Through: Mike Swanson, City Manager**  
**Scott Burgess, Community Development Director Pro-Tem**  
**Dennis Lively, Engineering Director**

**From: Jack R. Ostlund Jr., Associate Engineer**

**Subject: Volume Based Sewer Rate**

**Date: August 23, 2001 for September 4, 2001 City Council Meeting**

**Action Requested**

Adopt the attached resolution to change from a fixed to a volume based sanitary sewer rate.

**Background**

At the Council's direction at the February 1, 2000 council meeting, staff has contracted with the Financial Consulting Solutions Group (FCSG) to identify and to document policy and administrative issues relative to the conversion from a fixed sewer rate to a variable volume based sewer rate charge. Last year when the Council adopted the rate increase you received testimony from customers who believe that flat rates are not equitable. In addition, you stated that the sewer rate should promote water conservation. Staff presented FCSG's analysis report to the Citizen's Utility Advisory Board (CUAB) at a meeting on February 7, 2001. The report included customer water usage statistics. The usage patterns were used to select conceptual methods of determining possible rates based on volume of sanitary sewer use. The CUAB provided staff and the consultant with guidance in structuring a new rate structure.

**Discussion**

The City currently has a split rate structure. The City uses a flat fee billing system where all residential customers pay the same fee regardless of the volume of sewage produced. Commercial customers pay a variable charge based on their water consumption. The equity issue involves the question of how fair is it to charge all

customers the same fee when it can be determined from water billings that there is a broad band of sewer usage among different residential and commercial customers. The water conservation issue is that customers may use less water if they have to pay for water that is actually entering the city's sanitary system and being treated at the Kellogg Sewer Treatment Plant or being diverted to the City of Portland sewer system.

The CUAB has concluded that the City, as the sewage provider, should take steps to establish an equitable and fair method of billing its residential customers. This would be based on a rate structure that includes a partial flat fee to cover the cost of the infrastructure and a variable volume rate based on the actual amount of sewage being produced by each customer. The variable portion would be determined using the water usage records provided by the City's water billing contractor Springbrook Software. Four winter months would be used to establish the rate, to avoid billing for water that is used for irrigation that never reaches the sewage treatment plant. The proposed rate structure for the next 3 fiscal years is shown in the following tables:

For commercial accounts, the charge will continue to be based on actual usage as determined each month. For residential accounts, including low-income residential accounts, the volume on which the monthly charge is based shall be the average monthly volume for the four-month period ending March 30 of each year. The volume rate would remain in effect from April 1 (immediately following the four-month averaging period) through March 30 of the following year.

All fractions of a 100 cubic foot (ccf) unit are to be rounded down.

Fiscal Year 2001/2002

<u># of CCF</u>	<u>Single-Family</u>	<u>Commercial</u>
0	\$29.00	\$29.00
2	\$30.40	\$34.00
4	\$31.80	\$39.00
6	\$33.20	\$44.00
8	\$34.60	\$49.00
10	\$36.00	\$54.00
12	\$37.40	\$59.00
14	\$38.80	\$64.00
16	\$40.20	\$69.00
20	\$43.00	\$79.00
25	\$46.50	\$91.50
30	\$50.00	\$104.00

\*Each CCF of Usage is billed

<u>RATE STRUCTURE</u>	<u>2000/2001 CURRENT RATES</u>		<u>2001/2002 PROJECTED RATES</u>	
	<u>Fixed *</u>	<u>Volume (&gt;16 ccf)</u>	<u>Fixed *</u>	<u>Volume (per ccf)</u>
<u>Residential (Incl. MFR)</u>	<u>\$36.25</u>	<u>-</u>	<u>\$29.00</u>	<u>\$0.70</u>
<u>Low-Income Residential</u>	<u>\$16.81</u>	<u>-</u>	<u>\$14.50</u>	<u>\$0.35</u>
<u>Commercial</u>	<u>\$36.25</u>	<u>\$2.30</u>	<u>\$29.00</u>	<u>\$2.50</u>

\*Fixed Charge is imposed per unit for residential, per account for commercial

<u>RATE STRUCTURE</u>	<u>2002/2003 PROJECTED RATES</u>		<u>2003/2004 PROJECTED RATES</u>	
	<u>Fixed *</u>	<u>Volume (per ccf)</u>	<u>Fixed *</u>	<u>Volume (per ccf)</u>
<u>Residential (Incl. MFR)</u>	<u>\$22.00</u>	<u>\$ 1.40</u>	<u>\$15.00</u>	<u>\$2.10</u>
<u>Low-Income Residential</u>	<u>\$11.00</u>	<u>\$0.70</u>	<u>\$7.50</u>	<u>\$1.05</u>
<u>Commercial</u>	<u>\$22.00</u>	<u>\$2.75</u>	<u>\$15.00</u>	<u>\$2.95</u>

\*Fixed Charge is imposed per unit for residential, per account for commercial

### **Concurrence**

Staff supports the CUAB recommendation to use the combination of flat fee and variable volume fee method of billing all City sanitary sewer customers. Staff will provide the necessary staff support to carry out this mission if the Council adopts the recommended rate change. Finance staff participated in development of this rate structure.

### **Fiscal Impact**

This change in rate structure method is revenue neutral and does not include an increase in the total amount billed.

### **Work Load Impacts**

Staff that would be required to administer the program is estimated to be ½ FTE Accounting Technician. The estimated cost of adding this employee is \$20,000 per

year (salary plus benefits). Engineering, sewer, and finance staff will bring Council a recommendation on this position within two months of adoption.

### **Alternatives**

1. Adopt the recommended Flat Fee/Variable Volume Fee
2. Keep the existing rate structure
3. Ask Staff for more information

### **Recommendation**

Adopt alternative 1

### **Attachment**

1. Resolution



August 21, 2001

Honorable City Council  
City of Milwaukie  
10722 SE Main Street  
Milwaukie, OR 97222

Dear Honorable City Council,

FCS Group is pleased to provide the analysis and findings of the volume-based sewer rate study. The purpose of this study has been to evaluate the transition of residential sewer rates from a flat rate to a volume-based charge. In addition, we investigated and documented numerous administrative and policy issues related to such a transition. This study is a continuation of the sewer revenue requirement update completed in May of 2000. As such, it did not re-visit the levels of revenues needed. Instead, it has been based on a revenue-neutral transition in rate structure, overlaid by increases in rate revenues recommended in that earlier effort.

The volume-based sewer study consisted of several tasks.

**Collect and Develop Customer Statistics** – Customer statistics were provided by the City's Information Systems consultants, Springbrook Software. These were compiled to provide information including:

- ✓ Number of Accounts by Class
- ✓ Monthly Usage by Customer Class
- ✓ Number of Bills at each Usage Levels
- ✓ Individual Usage of Customers during a defined "Winter Period"

The data were also examined for validity by comparing the calculated revenues versus the actual revenues collected.

**Analyze the Patterns of Customer Usage** – Using the compiled customer data, each customer class' usage was diagramed and analyzed for patterns of use. The usage patterns were utilized to help answer several questions, such as: how valuable is it to switch to volume-based sewer rates; should the City use a customer's "Winter Average" versus his year-round usage; and what period of minimal usage is the appropriate "Winter Period"?

**Utilize the Citizens Utility Advisory Board to Narrow Rate Options** – Through a series of work sessions, we reviewed various rate options and policy issues and the pros and cons of each rate option with the Citizens Utility Advisory Board (CUAB). Materials such as issue papers and summary packets were sent to CUAB members prior to these work sessions for maximum efficiency. Copies of the issue papers developed and used in this process are included in Appendix A.

**Present Rates to the City Council** – Using the CUAB’s recommendations, we presented a set of rate options to the City Council. A copy of the presentation packet is included as Appendix B.

## **SUMMARY OF FINDINGS**

Through the process described above, a number of important issues were addressed leading to a recommended rate strategy. They include:

### **Validity of Customer Statistics**

FCS Group received and analyzed two sets of customer data from Springbrook Software, the City’s information systems consultants. The first set of customer data did not include customers who had zero water usage during any given bimonthly billing period. Preliminary analyses were developed by using this incomplete data set and normalizing it to fit known historical financial performance. The CUAB was uncomfortable with this approach, especially given the increased revenue risk which is inherent in volume-based rates, and through their direction, City staff worked with Springbrook to develop a valid and complete data set.

The second set of customer data was more complete. When the customer statistics was priced-out with the actual revenues, the difference was 1.15%. The deviation was not significant and was within our acceptable margin of error.

### **Patterns of Customer Usage**

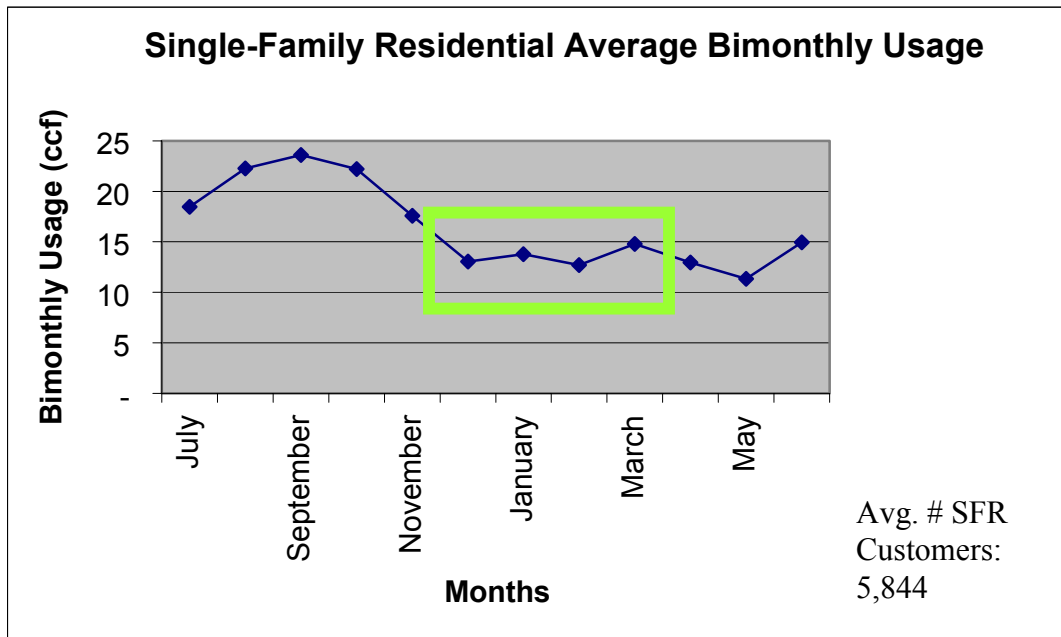
Volume-based sewer rates charge customers for the estimated amount of wastewater deposited in the system. In comparison to a fixed sewer rate, volume-based sewer rates increase equity among individual customers. Each customer is charged according to the demand they place on the system, and not the system average. Unlike the water system, which has water meters, there is no monitor for the exact amount of wastewater that a customer deposits into the system. Instead, a customer’s sewer volume average is approximated from their water usage.

“Winter Average” sewer rates assumes a customer’s winter usage is representative of the average wastewater flow for the entire year. This minimizes charging customers for irrigation or other outdoor water uses that do not enter the sewer system.

“Winter Averaging” also increases equity among customer classes. If all customers were billed based on their year-round usage, single-family customers, who as a class use a greater share of water for irrigation and other outdoor

consumption, would be overcharged for their wastewater disposal as compared to their sewage volumes.

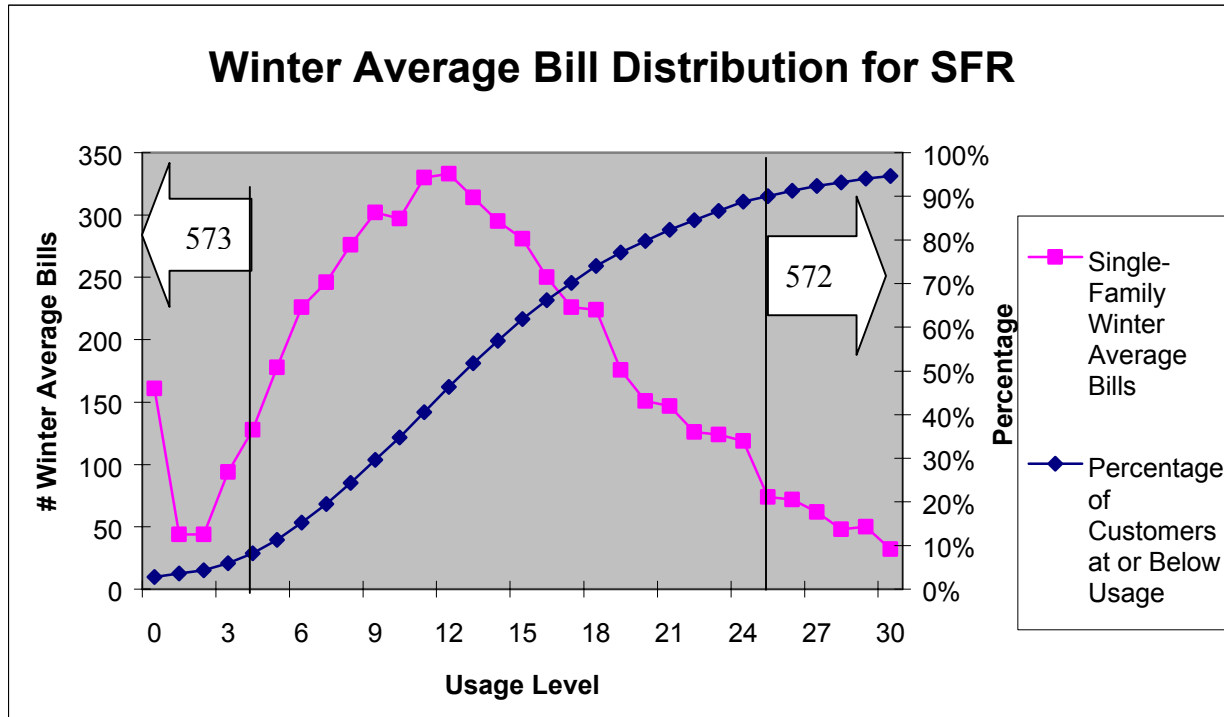
The “Winter Period” for “Winter Averaging” can be as short as a month to as long as six. Logically, we try to identify a period of very low stable usage and mark that period or series of months as the “Winter Average” period. After examining the graph below we identified the bimonthly billing periods ending from December to March as an appropriate “Winter Average” period. The CUAB concurred with this recommendation.



The customer statistics provided by Springbrook Software showed single-family and multi-family customers have peak water usage during the same summer months of the year. The main difference between Single and Multi-family customers is the magnitude of peak usage during the summer months. Whereas the average Single-Family customer may see their summer usage increase nearly 75% during the summer months, Multi-Family customers on average increase their summer usage by only 35%. Therefore, the case could be made that Multi-Family Residential customers could also be charged based on their “Winter Average” or based on year-round consumption. Both options were developed during this study. As noted below, the CUAB preferred to use “Winter Average” as the billing basis for all residential accounts.

In considering the transition to volume-based rates, customer impacts are an important element. While average rates and revenues remain constant, bills for individual customers can change profoundly. We examined the impact on individual customers should the City of Milwaukie switch to a “Winter Average” volume-based sewer rate. We found that while average winter use is between

fifteen hundred cubic feet (CCF), approximately ten percent of residential customers average more than 26 CCF and ten percent average less than six CCF during the “Winter Period” as defined above. The distribution of single-family customer averages is displayed below.



The graph displays the number of customers with “Winter Average” use at each usage level (line with square markers). The second line (line with diamond markers) displays the cumulative percentage of customers who average the level of usage or less. The graph shows 50% of the customers use approximately fourteen ccf or less. The average usage is approximately fifteen ccf. That means over half the customers would receive a discount with the volume based sewer rate structure versus the current fixed charge rate structure. At the same time, a significant fraction of customers use substantially more than the average, and could face substantial increases under a transition to volume-based rates.

### Utilize the Citizens Utility Advisory Board to Narrow Rate Options

Applying the analysis we’ve performed, we presented several rate options to the Citizens Utility Advisory Board (CUAB). Some of the options included the

- current fixed residential charge,
- a rate structure with a minimum usage,
- and a single fixed charge with a single volume charge.

The option the CUAB preferred was a single fixed charge with a single volume charge. The CUAB liked the clarity and simplicity of this structure, while the goal of rate equity is achieved in the most straightforward manner. In general, several

issues concerned the CUAB about the implementation of volume-based sewer rates, and guided their judgment regarding rate options and implementation. The CUAB was concerned

- rates may lead to instability in revenue generation,
- there would be confusion about the impact of the new rate structure,
- and high-volume users would be burdened with a large portion of the costs without adequate notification.

The CUAB suggested the volume portion of the rate revenue be phased-in. With a current charge of \$36 dollars the CUAB suggested reducing the fixed charge by seven dollars to \$29 leaving the remainder of the revenue requirement to be generated from the volume charge. The CUAB recommended reducing the fixed charge by seven dollars each year until it reached \$15 per month with approximately a \$2.10 volume-charge. At that time, the City could re-visit this issue and evaluate whether further rate adjustments are appropriate.

Multi-family customers have a usage pattern similar to single-family but have magnitudes of peaking that suggest irrigation is a much smaller percentage of the peak usage. The CUAB was asked if multi-family customers should be segregated from single-family and charged on a volume basis much like commercial customers. The CUAB preferred to retain the same rate structure for single-family and multi-family residential to maintain rate clarity. Therefore, both single-family and multi-family classes will be charged on the proposed “residential” volume-based structures.

The CUAB also asked that the City Council take into consideration the administrative costs of implementing volume-based sewer rates. The first year would require an additional \$10,000 of onetime costs (not including the cost of this study) with approximately half of a full-time employee to administer the program from implementation onward.

The CUAB also recommended that the City promote assistance programs (i.e. conservation programs) to high-volume users, especially for those with limited financial resources.

## **Present Rates to the City Council**

With the recommendations from the CUAB, the rates were presented to the City on March 19, 2001.

The results of this presentation can be summarized as follows:

- The City Council was impressed by the depth and breadth of review provided by the CUAB. The Council expressed general support for the CUAB recommendations.
- The Council was concerned about equitable treatment of customers with usage histories showing zero minimum volumes. They asked for options regarding zero volume accounts. A separate summary of this issue and available options has been provided.
- The Council also direct that the rate proposal submitted for adoption include scheduled rate increases identified in the May 2000 revenue requirements study.

In May of 2000, FCS Group recommended the City of Milwaukie implement a 7% increase followed by several 3.5% to 4.5% increases each year. The seven percent rate increase was implemented before the 2000-2001 fiscal year.

	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>
Annual	7.10%	3.59%	3.78%	4.50%
Cumulative	7.10%	10.43%	13.81%	17.69%

In executing the series of increases for fiscal years 2002 and beyond, the increased rate revenue has been targeted for recovery through a higher volume charge, while the decrease in the fixed charge maintains the CUAB's recommended schedule of \$7 reduction per year until it reaches \$15, at which point a volume charge of \$2.10 would apply.

The resulting rate structures are displayed in the following tables.

**City of Milwaukie – Sewer Rate Study**  
**June 5, 2001**  
**Final Report**

**2001-2002 Rates**

RATE STRUCTURE	2000/2001 CURRENT RATES		2001/2002 (3.59% Increase) PROJECTED RATES	
	Fixed *	Volume (> 16 ccf)	Fixed *	Volume (per ccf)
Residential (Incl. MFR)	\$ 36.25	\$ -	\$29.00	\$0.70
Low-Income Residential	16.81	-	\$14.50	\$0.35
Commercial	36.25	2.30	\$29.00	\$2.50

\*Fixed charge imposed per residential unit for residential and per account for commercial customers

In the 2000-2001 fiscal year commercial customers were given a 16 ccf allowance. This allowance would be discontinued under the new recommended rate structure.

**2002-2004 Rates**

RATE STRUCTURE	2002/2003 (3.78% Increase) PROJECTED RATES		2003/2004 (4.5% Increase) PROJECTED RATES	
	Fixed *	Volume (per ccf)	Fixed *	Volume (per ccf)
Residential (Incl. MFR)	\$22.00	\$1.40	\$15.00	\$2.10
Low-Income Residential	\$11.00	\$0.70	\$7.50	\$1.05
Commercial	\$22.00	\$2.75	\$15.00	\$2.95

The City could elect to adopt this entire rate transition package at this time, or solely adopt the 2001-2002 rates, now, and consider the subsequent revisions each year.

It has been a pleasure to work with the City staff, the CUAB, and City Council and we look forward to continuing the relationship in the future. Please feel free to call us with any questions, comments or concerns at (425) 867-1802.



**To: City Council**

**Through: Mike Swanson, City Manager**

**From: Alice Rouyer, Director of Community Development & Public Works**

**Subject: Strategy for extending City sewer service to unsewered areas in the Urban Growth Management Area.**

**Date: September 24, 2004 for the October 5, 2004 work session**

### **Action Requested**

Discuss strategies for extending City sewer service to areas in the Urban Growth Management Area. Strategies include discussion of recent sewer basin master planning in the unsewered area east of the City and phased annexations that would help accomplish future public sewer extensions.

### **Background**

Following the recent Hill Street annexation, staff met with counterparts at Water Environment Services (WES). The City needed to clarify roles with the County when reviewing building permits for new development in annexation areas. During that conversation, City staff sought a status report from the County regarding plans for sewer extensions in the area south of Johnson Creek Blvd., north of King Road and east of the City limits to Bell Avenue. The City has long desired to be the sewer provider in this area. This was memorialized in a County/City Urban Growth Management Agreement (UGMA) signed in July 1990. This area is identified in that agreement as Dual Interest Area "A" and is generally understood to be the City's first priority area for future annexation. Council approved three small annexations in this area in the past four years. The annexations were all requested by private property owners, and all have been completed.

Staff from WES indicated that they have consistently not permitted new sewer extensions into the area in order to reserve it for future City sewer service and annexation in accordance with the UGMA. They have no intention of reversing that policy. County staff did mention that they frequently get calls from residents with failing septic tanks or cesspools asking when public sewer might be available. This led to a conversation about

the City's plans for providing sewer service to this area in the future. Options are provided for sewer extension into Dual Interest Area "A" in the draft Sewer Master Plan update. The Council will be considering the Master Plan this fall. Staff will be prepared to discuss strategies for sewer service extensions into this area such as basin master planning and phased annexations in more detail at the October 5, 2004 work session.

## Proposed by Initiative Petition

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### MEASURE 37

#### **GOVERNMENTS MUST PAY OWNERS, OR FORGO ENFORCEMENT, WHEN CERTAIN LAND USE RESTRICTIONS REDUCE PROPERTY VALUE**

**RESULT OF "YES" VOTE:** "Yes" vote requires that governments pay owners, or forgo enforcement by repealing, changing, not applying restrictions, when certain land use restrictions reduce owners' property value.

**RESULT OF "NO" VOTE:** "No" vote rejects requiring that governments pay owners or forgo enforcement by repealing, changing, not applying restrictions, when certain land use restrictions reduce property value.

**SUMMARY:** Currently, Oregon Constitution requires government(s) to pay owner "just compensation" when condemning private property or taking it by other action, including laws precluding all substantial beneficial or economically viable use. Measure enacts statute requiring that when state, city, county, metropolitan service district enacts or enforces land use regulation that restricts use of private real property or interest thereon, government must pay owner reduction in fair market value of affected property interest, or forgo enforcement. Governments may repeal, change, or not apply restrictions in lieu of payment; if compensation not timely paid, owner not subject to restrictions. Applies to restrictions enacted after "family member" (defined) acquired property. Creates civil right of action including attorney fees. Provides no new revenue source for payments. Certain exceptions. Other provisions.

#### **ESTIMATE OF FINANCIAL IMPACT:**

The measure would require state administrative expenditures to respond to claims for compensation of between \$18 million and \$44 million per year.

The measure may require compensation to landowners. The amount of state expenditures needed to pay claims for compensation cannot be determined.

There is no financial effect on state revenues.

The measure would require local government administrative expenditures to respond to claims for compensation of between \$46 million and \$300 million per year.

The measure may require compensation to landowners. The amount of local government expenditures needed to pay claims for compensation cannot be determined.

The effect of the measure on local government revenues cannot be determined.

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BILL BRADBURY  
SECRETARY OF STATE



JOHN LINDBACK  
DIRECTOR

141 STATE CAPITOL  
SALEM, OREGON 97310-0722

ELECTIONS — (503) 986-1518

March 17, 2003

To All Interested Parties:

Secretary of State Bill Bradbury is responsible for the pre-election review of proposed initiative petitions for compliance with the procedural constitutional requirements established in the Oregon Constitution for initiative petitions. This review will be completed before approving the form of the cover and signature sheets for the purpose of circulating the proposed initiative petition to gather signatures.

The Secretary of State is seeking public input on whether proposed initiative petition (#36), satisfies the procedural constitutional requirements for circulation as a proposed initiative petition. Petition #36 was filed in our office on March 14, 2003, by Eugene Prete and Barbara Prete, for the General Election of November 2, 2004.

Enclosed is a copy of the text of this proposed initiative petition. If you are interested in providing comments on whether the proposed initiative petition meets the procedural constitutional requirements, please write to the secretary at the Elections Division in the State Capitol. Your comments, if any, must be received by the Elections Division no later than April 7, 2003, in order for them to be considered in the review.

BILL BRADBURY  
Secretary of State

BY: *Summer Davis*

Summer Davis  
Compliance Specialist



The following provisions are added to and made a part of ORS chapter 197:

- (1) If a public entity enacts or enforces a new land use regulation or enforces a land use regulation enacted prior to the effective date of this amendment that restricts the use of private real property or any interest therein and has the effect of reducing the fair market value of the property, or any interest therein, then the owner of the property shall be paid just compensation.
- (2) Just compensation shall be equal to the reduction in the fair market value of the affected property interest resulting from enactment or enforcement of the land use regulation as of the date the owner makes written demand for compensation under this act.
- (3) Subsection (1) of this act shall not apply to land use regulations:
  - (A) Restricting or prohibiting activities commonly and historically recognized as public nuisances under common law. This subsection shall be construed narrowly in favor of a finding of compensation under this act;
  - (B) Restricting or prohibiting activities for the protection of public health and safety, such as fire and building codes, health and sanitation regulations, solid or hazardous waste regulations, and pollution control regulations;
  - (C) To the extent the land use regulation is required to comply with federal law;
  - (D) Restricting or prohibiting the use of a property for the purpose of selling pornography or performing nude dancing. Nothing in this subsection, however, is intended to affect or alter rights provided by the Oregon or United States Constitutions; or
  - (E) Enacted prior to the date of acquisition of the property by the owner or a family member of the owner who owned the subject property prior to acquisition or inheritance by the owner, whichever occurred first.
- (4) Just compensation under subsection (1) of this act shall be due the owner of the property if the land use regulation continues to be enforced against the property 180 days after the owner of the property makes written demand for compensation under this section to the public entity enacting or enforcing the land use regulation.
- (5) For claims arising from land use regulations enacted prior to the effective date of this act, written demand for compensation under subsection (4) shall be made within two years of the effective date of this act, or the date the public entity applies the land use regulation as an approval criteria to an application submitted by the owner of the property, whichever is later. For claims arising from land

use regulations enacted after the effective date of this act, written demand for compensation under subsection (4) shall be made within two years of the enactment of the land use regulation, or the date the owner of the property submits a land use application in which the land use regulation is an approval criteria, whichever is later.

- (6) If a land use regulation continues to apply to the subject property more than 180 days after the present owner of the property has made written demand for compensation under this act, the present owner of the property, or any interest therein, shall have a cause of action for compensation under this act in the circuit court in which the real property is located, and the present owner of the real property shall be entitled to reasonable attorney fees, expenses, costs, and other disbursements reasonably incurred to collect the compensation.
- (7) A metropolitan service district, city, or county, or state agency may adopt or apply procedures for the processing of claims under this act, but in no event shall these procedures act as a prerequisite to the filing of a compensation claim under subsection (6) of this act, nor shall the failure of an owner of property to file an application for a land use permit with the local government serve as grounds for dismissal, abatement, or delay of a compensation claim under subsection (6) of this act.
- (8) Notwithstanding any other state statute or the availability of funds under subsection (10) of this act, in lieu of payment of just compensation under this act, the governing body responsible for enacting the land use regulation may modify, remove, or not to apply the land use regulation or land use regulations to allow the owner to use the property for a use permitted at the time the owner acquired the property.
- (9) A decision by a governing body under this act shall not be considered a land use decision as defined in ORS 197.015(10).
- (10) Claims made under this section shall be paid from funds, if any, specifically allocated by the legislature, city, county, or metropolitan service district for payment of claims under this act. Notwithstanding the availability of funds under this subsection, a metropolitan service district, city, county, or state agency shall have discretion to use available funds to pay claims or to modify, remove, or not apply a land use regulation or land use regulations pursuant to subsection (6) of this act. If a claim has not been paid within two years from the date on which it accrues, the owner shall be allowed to use the property as permitted at the time the owner acquired the property.
- (11) Definitions – for purposes of this section:
  - (A) “Family member” shall include the wife, husband, son, daughter, mother, father, brother, brother-in-law, sister, sister-in-law, son-in-law, daughter-in-law,

mother-in-law, father-in-law, aunt, uncle, niece, nephew, stepparent, stepchild, grandparent, or grandchild of the owner of the property, an estate of any of the foregoing family members, or a legal entity owned by any one or combination of these family members or the owner of the property.

(B) "Land use regulation" shall include:

- (i) Any statute regulating the use of land or any interest therein;
- (ii) Administrative rules and goals of the Land Conservation and Development Commission;
- (iii) Local government comprehensive plans, zoning ordinances, land division ordinances, and transportation ordinances;
- (iv) Metropolitan service district regional framework plans, functional plans, planning goals and objectives; and
- (v) Statutes and administrative rules regulating farming and forest practices.

(C) "Owner" is the present owner of the property, or any interest therein.

(D) "Public entity" shall include the state, a metropolitan service district, a city, or a county.

- (12) The remedy created by this act is in addition to any other remedy under the Oregon or United States Constitutions, and is not intended to modify or replace any other remedy.
- (13) If any portion or portions of this act are declared invalid by a court of competent jurisdiction, the remaining portions of this act shall remain in full force and effect.

RECEIVED  
03 MAR 14 PM 3 34  
BILL BRADY  
SECRETARY OF STATE

November 2, 2004 General Election

Ballot Measure 37

Explanatory Statement:

Ballot Measure 37 adds a new statute to ORS chapter 197. As specified in the measure, the owner of private real property is entitled to receive just compensation when a land use regulation is enacted after the owner or a family member became the owner of the property if the regulation restricts the use of the property and reduces its fair market value.

If a property owner proves that a land use regulation restricts the use of the owner's property, and reduces its value then the government responsible for the regulation will have a choice: pay the owner of the property an amount equal to the reduction in value or modify, change or not apply the regulation to the owner's property.

The measure allows the state, county, city or metropolitan service district to adopt procedures for processing claims for compensation, but prohibits those procedures from being treated as a prerequisite to the filing of a claim in circuit court.

The measure does not apply to commonly and historically recognized public nuisances, public health and safety regulations, regulations required to comply with federal law, and regulations restricting or prohibiting the use of a property for the purpose of selling pornography or performing nude dancing.

The measure specifies that compensation is due if the regulation remains in force 180 days after the owner makes written demand for compensation. After that time, the present owner may file an action in the circuit court in the county in which the property is located. The measure also specifies that the present owner is entitled to reasonable attorney fees, expenses, costs and other disbursements reasonably incurred to collect compensation.

The measure provides no new revenue source for payments, if any, required under this measure.

The measure defines several terms that are used in the statute including "family member" which is defined as wife, husband, son, daughter, mother, father, brother, brother-in-law, sister, sister-in-law, son-in-law, daughter-in-law, mother-in-law, father-in-law, aunt, uncle, niece, nephew, stepparent, stepchild, grandparent, or grandchild of the owner of the property, an estate of any of the foregoing family members, or a legal entity owned by any one or combination of these family members or the owner of the property.

HARDY MYERS  
Attorney General



PETER D. SHEPHERD  
Deputy Attorney General

DEPARTMENT OF JUSTICE  
GENERAL COUNSEL DIVISION

MEMORANDUM

DATE: July 19, 2004  
TO: Lane Shetterly, Jim Brown  
FROM: Richard Whitman, AIC Natural Resources Section  
SUBJECT: Initiative Petition 36

This office has been contacted by a number of state agencies seeking guidance in preparing fiscal impact statements for Initiative Petition 36 (IP 36). IP 36 is a proposed initiative that would provide, by statute, a supplemental right to just compensation to owners of real property when:

- A state or local public entity *enacts or applies* a law that restricts the use of that real property, or any interest in that property; and
- The enactment or application of the law has the effect of reducing the fair market value of the property;
- The governing body responsible for enacting the law in question does not modify, remove, or waive the law to allow the owner to use the property for a use permitted at the time the owner acquired the property.

The purpose of this memo is to provide limited preliminary legal guidance to state agencies that are preparing fiscal impact information concerning IP 36. I caution at the outset that there are some significant ambiguities in IP 36, particularly regarding its exemptions and under what circumstances public entities will have to pay compensation (as opposed to modifying or otherwise waiving the law that restricts the use of the property in question).

1. What Types of Laws May Require Compensation Under IP 36?

IP 36 defines what laws require compensation. The definition includes: *any statute* regulating the use of land or any interest therein; rules and goals of LCDC; local land use and transportation ordinances; certain enactments of Metro; and statutes and rules regulating farm and forest practices. The scope of IP 36 is further illustrated by the exceptions listed in the measure. Those exceptions include laws for protecting public health and safety (including building codes); laws restricting or prohibiting the use of property to sell pornography or for nude dancing; and laws restricting or prohibiting historically recognized nuisances. Thus, the

Jim Brown, Lane Shetterly  
July 22, 2004  
Page 2

application of IP 36 appears to be very broad. Any state or local law that regulates how land (or any interest in land) is used appears to be encompassed by the measure. This would include both laws that govern what purposes property interests may be used for (such as zoning laws, state laws restricting certain uses based on their proximity to schools or religious institutions, state scenic waterway laws), and laws that govern how a particular use of real property may be carried out (such as highway access controls, height limits, density requirements, mined land reclamation laws, mobile home park laws, landlord/tenant laws, subdivision laws and forest and agricultural practice laws).<sup>1</sup>

## 2. Exemptions

As noted above, after providing that any law that restricts the use of private real property and that has the effect of reducing that property's value creates a right to compensation, IP 36 then sets forth a series of exemptions that take certain types of laws back out of body of laws that can trigger payment. Three of the five exemptions in IP 36 are very similar to the exemptions that would have been provided under 2000 Oregon Ballot Measure 7, which also would have created a supplemental right to compensation. At this point in time, I recommend that state agencies looking for guidance concerning the meaning of these three exemptions look to the Attorney General opinion on Measure 7. 49 Op Att'y Gen 284 (2001).

Two of the five exemptions in IP 36 are new, relative to 2000 Ballot Measure 7. The first would exempt laws restricting or prohibiting activities for the protection of public health and safety, such as fire and building codes, health and sanitation regulations, solid or hazardous waste regulations, and pollution control regulations. As an initial matter, and subject to further analysis, this exemption appears to apply to many regulations of the Department of Environmental Quality, the Health Division, the Department of Agriculture (Food Safety programs), Oregon OSHA, DCBS/Building Codes, among others. In general, the exemption appears premised on a distinction between laws enacted to promote the public welfare, and laws that are designed for public health and safety purposes. The distinction between these two areas is likely to be an area of significant dispute and uncertainty.

The second new exemption is specific to how particular laws relate to the owner(s) of a particular property. Compensation is not required where the law in question was enacted "prior to the date of acquisition of the property by the owner or [by] a family member of the owner \* \* \*." A "family member" is defined to include, among other things, " \* \* \* a legal entity owned by any one or combination of \* \* \* family members or the owner of the property." Thus, for example, if the property in question was at one time owned by a corporation, and the current owner's grandfather owned stock in that corporation, then under IP 36 it appears that the current owner has a right to compensation for any law enacted after the date that corporation acquired the property. Again, this is an area of some uncertainty, and is likely to be a source of significant dispute concerning IP 36.

<sup>1</sup> The laws listed are intended to be illustrative, not an exhaustive list of the types of laws that could create a right to compensation.

Jim Brown, Lane Shetterly  
July 22, 2004  
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### 3. Waiver Versus Payment

Subsections (8) and (10) of IP 36 provides that

(8) Notwithstanding any other state statute or the availability of funds under subsection (10) of this act, in lieu of payment of just compensation under this act, the *governing body* responsible for *enacting* the land use regulation *may* modify, remove, or [act] not to apply the land use regulation or land use regulations to allow the owner to use the property for a use permitted at the time the owner acquired the property.

\* \* \*

(10) Claims made under this section shall be paid from funds, if any, specifically allocated by the legislature, city, county or metropolitan service district for payment of claims under this act. *Notwithstanding the availability of funds under this subsection*, a metropolitan service district, city, county, or state agency shall have *discretion to use available funds to pay claims or to modify, remove, or not apply a land use regulation or land use regulations* \* \* \*. If a claim has not been paid within two years from the date on which it accrues, the owner shall be allowed to use the property as permitted at the time the owner acquired the property."

Read together, subsections (8) and (10) of IP 36 appear to require a public entity to waive or otherwise act to not apply a law that is the basis for a claim, unless funds have been appropriated by the legislative body for the entity for the specific purpose of paying claims. It should be noted, however, that subsection (8) only gives authority to waive a law to the *governing body responsible for enacting the law that gives rise to a claim*. Thus, for example, for statutes that restrict the use of private real property, only the state legislative could waive the law. Similarly, local governments would not have the authority to waive state statutes or rules that they are required to apply to their decisions. ORS 197.646.

The fact that IP 36 provides for claims against a public entity that applies a law, even if that entity did not enact that law, creates significant uncertainty about how the measure will be implemented. As a general matter, I recommend that state agencies assume that they would incur liability for statutes that they are responsible for administering. For administrative rules, where an agency is given the authority to waive under IP 36, my preliminary recommendation is that state agencies assume that they will be required to waive the law in the absence of any specific legislative appropriation. Thus, for state laws, agencies should assume no waiver of statutes, and that waiver of state rules is required unless the legislature acts to appropriate funds to pay claims under IP 36.

Jim Brown, Lane Shetterly  
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One final complication in the area of land use laws is that, under almost all circumstances, state statutes and administrative rules that regulate land use are "applied" by local governments that make land use decisions. IP 36 would appear to allow a claim against the state as the entity that "enacts" such laws. At the same time, IP 36 also would appear to allow a claim against the local government entity that "applies" such laws. This raises significant uncertainties both for state government, and for local governments, concerning how liability and authority to waive would be allocated as between the two. At this preliminary stage, we can't conclude with any certainty that the state would not be liable for local actions that implement state law. Nor can we conclude with any certainty that local governments would not be liable for the cost of compensating for state laws that they are unable to modify or otherwise waive. We will continue to review this issue, but it is clearly an extremely significant internal ambiguity in IP 36.

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DRAFT



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EXECUTIVE DIRECTOR

Ken L. Strobeck

To: Financial Impact Statement Committee Members  
From: Linda Ludwig, League of Oregon Cities  
RE: Estimated Financial Impact of Initiative 36  
Date: July 28, 2004

The League has reviewed Initiative #36 in order to ascertain costs to local governments that would be associated with the initiative if it were to pass in the November election. **It is easy to see that the costs of Initiative #36 would be substantial-** when comparing the initiative to methodology that was used to evaluate the local government fiscal impacts of a prior but essentially similar ballot measure, Measure 7.

**We believe that, if passed, Initiative #36 will result in claim costs to local government resembling Measure 7's conservative estimates at \$3.8 billion per year. Additionally, the League has ascertained that there would be additional administrative costs to local governments in the range of \$162 - 830 million per year.**

Essentially, the intent and the language of the measures is similar- creating a process for property owners to seek compensation when state or local regulations diminish property value. Although #36 provides additional exclusions and a waiver provision that was not explicit in #7, it allows for a broader set of potential claimants from multiple generations of family members of the current owner- likely resulting in costlier claims.

Additionally, as purveyors of good public policy, local governments will likely need to make an assessment of each claim, whether to pay or to waive, and the ramifications of both decisions. This process at a minimum would include ownership research, costs of an appraisal that makes multiple value determinations, staff reports, assessments of impacts to neighbors, assessments of collateral impacts to infrastructure investments, legal assistance and public hearings. The result would be significant costs to local governments even if the claim is waived or denied.

There would also potentially be costs to local governments that have been previously borne by developers, such as collateral costs when a local government waived a regulation that put additional unplanned capacity on infrastructure systems or open space requirements. Financing these costs often currently occur through system development

charges or other mechanisms currently paid by largely the developer that don't directly place the burden on the individual taxpayer.

The magnitude of claim liability for this initiative is difficult to determine- but we know it would be substantial. ECONorthwest prepared a entitled "Fiscal Impacts of Ballot Measure 7 on State and Local Governments: An Analysis of Selected Regulations," in which their nine case studies resulted in \$9-16 billion in compensation claims. Additionally, shortly after Measure 7 passed, Jackson County received a single compensation claim for over \$5 million.

Oregon has approximately 27,000,000 acres of private property. If an average parcel size was 10 acres- both inside and outside the urban growth boundary- and 1% of the property owners filed and received compensation in the amount of \$150,000, it would cost local governments \$4.5 billion per year in claims costs alone. Or, if 5% of the property owners received compensation in the amount of \$28,000, it would cost local governments approximately \$4 billion per year in claims costs<sup>a</sup>. These amounts of claims and/or compensation liability are very small considering the potential both in terms of numbers of claims or costs of compensation.

Utilizing these same parcel and claim rate assumptions, administrative costs to process claims will cost local governments from \$162- 830 million dollars per year under this initiative.<sup>b</sup>

A more detailed comprehensive fiscal analysis of the proposed statutory amendment would require a through analysis of potential claims for each individual property in a control group. Additionally, in order to determine the complete costs of the initiative, an analysis would be required of a new administrative process that local government would likely enact in order to make the claim determination necessary under the language of the initiative.

**Without a comprehensive property-by-property type analysis, we believe the estimates of claim costs for Initiative #36 in the amount of \$3.8 billion per year and administrative costs in the amount of \$162- 830 million per year to be reasonable.**

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<sup>a</sup> These figures assume acres inside urban growth boundaries as 740,560; outside urban growth boundaries as follows: farm zoned, 15.5 million; forest and farm/forest, 10.5 million, rural/other rural, 1 million. Average density rates are assumed as follows; inside urban growth boundaries, 4 parcels per acre; farm zoned, 80 acres per parcel; forest and farm/forest, 300 acres per parcel; rural/other rural, 10 acres per parcel.

<sup>b</sup> These figures assume an average claim cost at \$6,000 for appraisals, assessment, and processing.